Legislative Audit Division

State of Montana

Report to the Legislature

December 2006

Financial-Compliance Audit

For the Two Fiscal Years Ended June 30, 2006

Public Employees' Retirement Board

Department of Administration
A component unit of the state of Montana

We performed a financial-compliance audit of the Public Employees' Retirement Board for the two fiscal years ended June 30, 2006. This report contains two recommendations relating to:

- **The actuarial soundness of three retirement systems.**
- **Reconciliation controls over external investments.**

This report also contains the financial statements and our independent auditor's report on the Public Employees' Retirement Board for the fiscal year ended June 30, 2006. The financial audit of the Public Employees' Retirement Board's financial statements for the fiscal year ended June 30, 2005, was issued in a separate report in November 2005 (05-08).

Direct comments/inquiries to:
Legislative Audit Division
Room 160, State Capitol
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06-08

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Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2007, will be issued by March 31, 2008. The Single Audit Report for the two fiscal years ended June 30, 2005, was issued on March 6, 2006. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
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December 2006

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the Public Employees' Retirement Board (PERB), a component unit of the state of Montana, for the two fiscal years ended June 30, 2006. Included in this report are recommendations related to the actuarial soundness of three retirement systems and reconciliation controls over external investments.

We issued an unqualified opinion on PERB's financial statements for the fiscal year ended June 30, 2006. Our audit opinion on the financial statements is also contained in PERB's Comprehensive Annual Financial Report. Copies of the PERB's annual report for fiscal year 2005-06 can be obtained from the Montana Public Employee Retirement Administration (MPERA). The annual report contains background, statistical, and actuarial information that is not included in this audit report which may be of interest to legislators or the public.

The written response to the audit recommendations is included at the end of the audit report. We thank the executive director and her staff for their assistance and cooperation throughout the audit.

Respectfully submitted,

/s/ Scott A. Seacat

Scott A. Seacat
Legislative Auditor

Room 160 · State Capitol Building · PO Box 201705 · Helena, MT· 59620-1705
Phone (406) 444-3122 · FAX (406) 444-9784 · E-Mail lad@mt.gov

Legislative Audit Division

Financial-Compliance Audit
For the Two Fiscal Years Ended June 30, 2006

Public Employees' Retirement Board

Department of Administration
A component unit of the state of Montana

Members of the audit staff involved in this audit were
Jeane Carstensen-Garrett, Brenda Kedish, Delsi Plummer, and
Sonia Powell.

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Public Employees' Retirement Board

		Term Expires
Carole Carey, President	Ekalaka	3/31/07
John Paull, Vice President	Butte	3/31/10
Robert Griffith	Helena	3/31/08
N. Jay Klawon	Hamilton	3/31/09
Troy McGee	Helena	3/31/08
Elizabeth Nedrow	Billings	3/31/11
Terrence Smith	Big Sky	3/31/09

Administrative Officials

Roxanne Minnehan, Executive Director

Kim Flatow, Member Services Bureau Chief

Barbara Quinn, Fiscal Services Bureau Chief

Kathy Samson, Defined Contribution Plans & Educational Services Bureau Chief

For additional information concerning the Montana Public Employees' Retirement Board, contact:

Roxanne Minnehan, Executive Director
100 North Park Avenue, Suite 200
PO Box 200131
Helena MT 59620-0131
(406) 444-3154
e-mail: rminnehan@mt.gov

Public Employees' Retirement Board

This report contains the results of our financial-compliance audit of the Public Employees' Retirement Board (PERB) for the two fiscal years ended June 30, 2006. We issued an unqualified opinion on the financial statements for the fiscal year ended June 30, 2006. This means the reader can rely on the financial information presented. The financial audit of the PERB for the fiscal year ended June 30, 2005, was issued in a separate report (05-08).

Montana Public Employee Retirement Administration (MPERA) personnel prepared PERB financial statements from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) with adjustment. Adjustments are made to accurately present financial activity.

The financial-compliance audit report for the two fiscal years ended June 30, 2004, contained four recommendations to the PERB. The recommendations addressed seeking legislation to actuarially fund three of the retirement systems, compliance with the constitutional requirement prohibiting diversion of assets, laws governing PERS Defined Contribution Retirement Plan (DCRP) contribution transfers and allocations, and investment reconciliation controls. We determined the PERB implemented three of the recommendations and partially implemented one. The recommendation partially implemented is related to investment reconciliation controls and is discussed on page 9.

During our financial-compliance audit for the two fiscal years ended June 30, 2006, we also reviewed the prior audit recommendation from the fiscal year 2004-05 financial audit and determined the recommendation was not implemented as discussed on page 5 of this report.

The listing below serves as a means of summarizing the recommendations contained in the report, the board's response thereto, and a reference to the supporting comments.

Report Summary

Recommendation #1	We recommend legislation be enacted for funding changes to ensure the PERS-DBRP, SRS, and GWPORS are funded on an actuarially sound basis, as required by the Montana Constitution and state law. 9
	Board Response: Concur. See page B-3
Recommendation #2	We recommend the PERB reconcile the PERS-DCRP and 457 plans external investment reports to SABHRS and resolve all differences... 10
	Board Response: Concur. See page B-4.

Introduction

We performed a financial-compliance audit of the Public Employees' Retirement Board (PERB) for the two fiscal years ended June 30, 2006. The objectives of our audit were to:

1. Determine if PERB complied with applicable laws and regulations.
2. Obtain an understanding of PERB's control systems and, if appropriate, make recommendations for improvement in internal and management controls of the PERB.
3. Determine if PERB's financial statements fairly present the results of operations for the fiscal year ended June 30, 2006.
4. Determine the implementation status of prior audit recommendations.

Our financial audit of the PERB's financial statements for the fiscal year ended June 30, 2005, was issued in a separate report in November 2005 (05-08).

Montana Public Employees' Retirement Administration (MPERA) prepares PERB's financial statements from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) with adjustment. Adjustments are made to accurately present financial activity to the readers of the statements.

This report contains two recommendations. Other areas, if any, of concern deemed not to have a significant effect on the successful operation of PERB are not specifically included in the report, but have been discussed with management. In accordance with section 5-13-307, MCA, we analyzed the cost of implementing the recommendations contained in this report and determined recommendation #1 was significant and is discussed in the report section on page 5.

Background

The PERB is a component unit of the state of Montana. A component unit is a legally separate organization for which the state of Montana is financially accountable. The PERB has exclusive control of the funds of eight retirement systems, including the

Volunteer Firefighters' Compensation Act, as well as the Section 457 Deferred Compensation Plan. The PERB governs MPERA, which is responsible for daily administration of the retirement systems. The governor appoints the seven board members to five-year terms.

Defined Benefit Pension Trust Funds

PERB manages the activities of the following defined benefit pension trust funds:

- Public Employees' Retirement System-Defined Benefit Retirement Plan (PERS-DBRP)
- Judges' Retirement System (JRS)
- Highway Patrol Officers' Retirement System (HPORS)
- Sheriffs' Retirement System (SRS)
- Game Wardens' and Peace Officers' Retirement System (GWPORS)
- Municipal Police Officers' Retirement System (MPORS)
- Firefighters' Unified Retirement System (FURS)
- Volunteer Firefighters' Compensation Act (VFCA)

These funds provide pension, disability, and death benefits to eligible members. The monthly benefits are based on years of service and salary levels while still employed. The Volunteer Firefighters' Compensation Act provides pension, disability, and death benefits to volunteer firefighters who are members of eligible Montana volunteer fire companies. Monthly benefits are based on years of service.

Defined Contribution Pension Trust Funds

PERB manages the activities of the following defined contribution pension trust funds:

- Public Employees' Retirement System-Defined Contribution Retirement Plan (PERS-DCRP)
- Section 457 Deferred Compensation Plan (457 Plan)

The PERS-DCRP holds the PERS contributions attributable to the employee and allows the employee to invest the contributions at his or her discretion, within approved investments. The 457 Plan allows employees to set aside a portion of their salary each payday toward retirement while deferring state and federal income taxes until future years. Employees participating in these two plans have two investment options:

- the fixed option, which guarantees both principal (contributions) and a pre-established quarterly rate of earnings;
- the variable option, which consists of numerous mutual funds.

Participating employees are allowed to invest in both the fixed and variable options. Those participating in the variable option may invest in as many offered funds as desired.

Withdrawal of deferred compensation funds is only available to employees upon separation from service, retirement, death, or upon an unforeseeable emergency meeting IRS-specified criteria while still employed. Withdrawals from PERS-DCRP are available upon termination of a PERS covered position.

Prior Audit Recommendations

The financial-compliance audit report for the two fiscal years ended June 30, 2004, contained four recommendations to the PERB. The recommendations addressed seeking legislation to actuarially fund three of the systems, compliance with the constitutional requirement prohibiting diversion of assets, laws governing PERS-DCRP contribution transfers and allocations, and investment reconciliation controls. We determined the PERB implemented three of the recommendations and partially implemented one. The recommendation partially implemented is related to investment reconciliation controls and is discussed on page 9.

During our financial-compliance audit for the two fiscal years ended June 30, 2006, we also reviewed the prior audit recommendation from the 2004-05 financial audit and determined the recommendation was not implemented as discussed on page 5 of this report.

Three Retirement Systems Actuarially Unsound

The Public Employees' Retirement System – Defined Benefit Retirement Plan (PERS-DBRP), Sheriffs' Retirement System (SRS), and Game Wardens' and Police Officers' Retirement System (GWPORS), continue to be actuarially unsound, based on the June 30, 2006, actuarial valuations.

As part of our prior audit, we recommended that legislation be enacted for funding changes to ensure the PERS-DBRP, SRS, and GWPORS are funded on an actuarially sound basis, as required by Article VIII, Section 15 of the Montana Constitution. A defined benefit retirement system is defined in state law as being actuarially sound when its contributions are sufficient to pay full actuarial cost of the plan over a period of up to 30 years. Based on the actuarial valuation dated June 30, 2006, the above systems still have an Unfunded Actuarial Accrued Liability (UAAL) that will not be amortized over a 30-year period.

The current maximum UAAL systems are able to pay off over 30 years are as follows: PERS $269.9 million, GWPORS $5.1 million, and SRS $(5.0) million. The negative $5 million for SRS indicates that the current employer and employee contributions do not cover the current costs of the system.

The following table shows the current UAAL, based on the June 30, 2006, actuarial valuations, and years to amortize the UAAL.

Table 1

Unfunded Actuarial Accrued Liability (Expressed in Thousands)

Valuation Date	PERS-DBRP	Years	SRS	Years	GWPORS	Years
7/01/2000	(251,540)	30	(26,002)	30	(5,544)	30
7/01/2002	983	0.1	(16,965)	30	379	*
7/01/2004	466,798	*	7,586	*	5,100	45.9
7/01/2005	540,988	*	10,889	*	5,453	49.5
6/30/2006	460,229	*	8,838	*	5,370	32.5

( ) Amounts in parentheses indicates no unfunded actuarial accrued liability.
** Does not amortize.*
Source: Compiled by the Legislative Audit Division from actuarial reports.

Based on the June 30, 2006, actuarial valuation, current employer contribution percentages would need to increase by the following percentage points in order to amortize the UAAL within a 30-year amortization period:

PERS-DBRP:	1.01%; from 6.9% to 7.91%
SRS:	1.84%; from 9.535% to 11.375%
GWPORS:	.04%; from 9% to 9.04%

The actuary continues to attribute the unfunded liability of the systems primarily to investment returns below the actuarial assumptions of eight percent for the three systems.

Because the underlying calculations in the actuarial valuation are long-term in nature, for actuarial purposes the systems smooth out short-term fluctuations in the market value of assets. The asset smoothing method recognizes the gains or losses over a 4-year period. The following tables depict the gain or losses that have been, or will be, recognized.

Table 2

Montana Public Employee Retirement Administration
Schedule of Investment Gain/(Loss) Recognition PERS-DBRP
(Expressed in Thousands)

Fiscal Year	Market Value Investment Gain/(Loss) Over Expected	2003	2004	2005	Investment Gain/(Loss) Recognition Current Year 2006	2007	2008	2009
1998	179,839							
1999	98,762							
2000	(3,881)	(970)						
2001	(385,081)	(96,270)	(96,270)					
2002	(425,030)	(106,258)	(106,258)	(106,258)				
2003	(38,134)	(9,534)	(9,534)	(9,534)	(9534)			
2004	143,930		35,983	35,983	35,983	35,983		
2005	1,317			329	329	329	329	
2006	32,120				8,030	8,030	8,030	8,030
2007	*					*	*	*

**Gain/(Loss) not yet known.*

Source: Compiled by the Legislative Audit Division from MPERA Personnel.

Table 3

Montana Public Employee Retirement Administration
Schedule of Investment Gain/(Loss) Recognition SRS
(Expressed in Thousands)

Fiscal Year	Market Value Investment Gain/(Loss) Over Expected	2003	2004	2005	Investment Gain/(Loss) Recognition Current Year 2006	2007	2008	2009
1998	7,935							
1999	4,615							
2000	(1,463)	(366)						
2001	(16,814)	(4,204)	(4,204)					
2002	(19,133)	(4,783)	(4,783)	(4,783)				
2003	(1,121)	(280)	(280)	(280)	(280)			
2004	6,435		1,609	1,609	1,609	1,609		
2005	100			25	25	25	25	
2006	1,342				336	336	336	336
2007	*					*	*	*

***** *Gain/(Loss) not yet known.*

Source: Compiled by the Legislative Audit Division from MPERA Personnel.

Table 4

Montana Public Employee Retirement Administration
Schedule of Investment Gain/(Loss) Recognition GWPORS
(Expressed in Thousands)

Fiscal Year	Market Value Investment Gain/(Loss) Over Expected	2003	2004	2005	Investment Gain/(Loss) Recognition Current Year 2006	2007	2008	2009
1998	2,038							
1999	1,167							
2000	(400)	(100)						
2001	(4,364)	(1,091)	(1,091)					
2002	(5,323)	(1,331)	(1,331)	(1,331)				
2003	(179)	(45)	(45)	(45)	(45)			
2004	1,941		485	485	485	485		
2005	(82)			(21)	(21)	(21)	(21)	
2006	275				69	69	69	69
2007	*					*	*	*

***** *Gain/(Loss) not yet known.*
Source: Compiled by the Legislative Audit Division from MPERA Personnel.

PERB did seek legislation for funding changes and during the fiscal year 2005 special session, a one-time contribution of $25 million was made to the PERS-DBRP plan to help offset the Unfunded Actuarial Accrued Liability (UAAL). Although this contribution helped reduce the UAAL for the PERS-DBRP system, current assets remain insufficient to fund the UAAL over a 30-year amortization period, for this system, as well as the SRS and GWPORS systems.

PERB should continue to work with the legislature to adopt and implement a funding change to ensure the systems are funded on an actuarially sound basis, in order to comply with the Montana Constitution and state law.

Recommendation #1
We recommend legislation be enacted for funding changes to ensure the PERS-DBRP, SRS, and GWPORS are funded on an actuarially sound basis, as required by the Montana Constitution and state law.

Investment Reconciliation Controls

PERB has unreconciled balances identified between the external investment reports and balances recorded on SABHRS for the defined contribution plans it administers.

PERB contracts with external investment managers and plan administrators to invest the PERS-DCRP and 457 plan participant contributions. Reports are provided to the board each quarter showing the investment earnings, investment fees, contributions, and withdrawals, as well as the ending balance of the investments.

As part of our audit, we reviewed the reconciliations performed by MPERA staff. The reconciliations identified investments for the fixed and mutual 457 deferred compensation plans differing from SABHRS by approximately $10 million and investments for the PERS-DCRP differed from SABHRS by $13,632. We found that the balance in the Defined Contribution Fixed Fund Appreciation/Depreciation account, as of June 30, 2006, was understated by approximately $6.5 million. Staff explained that when they recorded each quarter's activity, they erroneously added the totals together, rather than increasing or decreasing the previous quarter's balance to obtain the cumulative changes shown on the report. In addition to this error, we noted the costs of the investments, as shown on SABHRS, were approximately $3.5 million less than that shown on the external reports. MPERA staff are unsure whether the costs of the investments are correctly recorded on SABHRS.

MPERA staff have identified, but not resolved differences in these reconciliations at fiscal years-end 2004, 2005, and 2006. Staff stated they are in the process of reviewing prior balances to determine the reasons for the differences noted. They indicated staff turnover has contributed to these unresolved differences. As of October 27, 2006, PERB has not resolved these discrepancies.

An effective control system includes a timely reconciliation of the investment balances on the accounting system to the external investment reports.

Recommendation #2
We recommend the PERB reconcile the PERS-DCRP and 457 plans external investment reports to SABHRS and resolve all differences.

Independent Auditor's Report, The Public Employees' Retirement Board's Management's Discussion and Analysis, Financial Statements, Required Supplementary Information, and Supplementary Information

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor

Deputy Legislative Auditors:
James Gillett
Jim Pellegrini

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Fiduciary Net Assets – Pension Trust Funds of the Public Employees' Retirement Board, a component unit of the state of Montana, as of June 30, 2006, and the related Statement of Changes in Fiduciary Net Assets – Pension Trust Funds for the year ended June 30, 2006. These financial statements are the responsibility of the Public Employees' Retirement Board. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Public Employees' Retirement Board as of June 30, 2006, and the changes in fiduciary net assets for the fiscal year then ended, in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis, the Schedule of Funding Progress, and the Schedule of Employer Contributions & Other Contributing Entities are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

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Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the Public Employees' Retirement Board. The Schedules of Administrative Expenses, Investment Expenses, and Consultants; the Detail of Fiduciary Net Assets (PERS-DBRP and PERS-DBEd) and the Detail of Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and PERS-DC Disability) as of June 30, 2006; and the related Detail of Changes in Fiduciary Net Assets (PERS-DBRP and PERS-DBEd) and the Detail of Changes in Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and PERS-DC Disability) for the fiscal year then ended are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

At July 1, 2006, three systems, Public Employees' (PERS-DBRP), Game Warden's Peace Officers' (GWPORS), and Sheriffs' (SRS) retirement systems were not actuarially sound with an Unfunded Actuarially Accrued Liability (UAAL) totaling $460.2 million, $5.3 million, and $8.8 million, respectively. The maximum UAAL to comply with the amortization period of 30 years at June 30, 2006, is $269.9 million for PERS-DBRP, $5.1 million for GWPORS, and $(5) million for SRS. The negative $5 million for SRS indicates that the current employer and employee contributions do not cover the current costs of the system.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

November 2, 2006

The Public Employees' Retirement Board's Management's Discussion and Analysis, Financial Statements, Required Supplementary Information, and Supplementary Information

Public Employees' Retirement Board

A Component Unit of the State of Montana

Management's Discussion and Analysis

This section presents management's discussion and analysis of the Montana Public Employees' Retirement Board's financial presentation and performance of the plans administered by the Board for the year ending June 30, 2006.

Financial Highlights

- *The Montana Public Employees' Retirement Board's combined total net assets of the defined benefit plans increased by $342.1 million or 8.7 percent in fiscal year 2006. The increase was primarily due to the investment income in each of the plans and the $25 million lump sum received from the State of Montana General Fund.*

- *The Montana Public Employees' Retirement Board's defined contribution plans combined total net assets increased by $15.3 million or 5.8 percent in fiscal year 2006. The total increase in Net Assets was due to investment income and contributions in both the DCRP and the 457 plan.*

- *Revenues (additions to plan net assets) for the Board's defined benefit plans for fiscal year 2006 was $556.1 million, which includes member and employer contributions of $203.1 million and net investment income of $352.9 million.*

- *Revenues (additions to plan net assets) for the Board's defined contribution plans for fiscal year 2006 was $29.4 million, which includes member and employer contributions of $23.7 million and net investment income of $5.7 million.*

- *Expenses (deductions to plan net assets) for the Board's defined benefit plans increased from $200.5 million in fiscal year 2005 to $214.0 million in fiscal year 2006 or about 6.7 percent. The increase in 2006 is primarily due to an increase in total benefit recipients and plan expenses.*

- *Expenses (deductions to plan net assets) for the Board's defined contribution plans decreased from $18.9 million in fiscal year 2005 to $14.4 million in fiscal year 2006 or about 23.6 percent. The decrease in expenses is primarily due to a decrease in distributions.*

- *The Montana Public Employees' Retirement Board's defined benefit plans funding objective is to meet long-term benefit obligations. As of June 30, 2006, the date of the latest actuarial valuation, three of the defined benefit plans were not able to pay off the unfunded liabilities over 30 years or less. As a whole the plans were actuarially funded at an average of 86 percent. It is important to understand this measure reflects the actuarial value of the defined benefit plans' net assets, which is less than the actual fair value published in the financial statements. Investment earnings are critical to the defined benefit plans and the market decline and associated investment* *losses in fiscal years 2001 and 2002 have had major impacts on the plans due to the smoothing of market value gains and losses over four years. In 2005 the last part of the 2002 investments loss was recognized. The PERB introduced legislation in the 2005 Legislative Session; however, no legislation was passed to correct the funding problem. The Public Employees' Retirement Board is committed to work with the 2007 Montana Legislature to resolve the funding issues of the PERS, GWPORS and SRS.*

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Public Employees' Retirement Board's (PERB) financial reporting which is comprised of the following components:

(1) Financial Statements
(2) Notes to the Financial Statements
(3) Required Supplementary Information

Collectively, this information presents the combined net assets held in trust for pension benefits for each of the plans administered by the Public Employees' Retirement Board as of June 30, 2006. This financial information also summarizes the combined changes in net assets held in trust for pension benefits for the year then ended. The information in each of these components is briefly summarized as follows:

(1) Financial Statements. For the fiscal year ended June 30, 2006, financial statements are presented for the fiduciary funds administered by the PERB. Fiduciary funds are used to account for resources held for the benefit of parties outside of the PERB. The fiduciary funds are held for participants in eight defined benefit plans and two defined contribution plans.

- The Statement of Fiduciary Net Assets is presented for the pension trust funds at June 30, 2006. These financial statements reflect the resources available to pay benefits to retirees and beneficiaries, at the end of the year reported.

- The Statement of Changes in Fiduciary Net Assets is presented for the pension trust funds for the year ended June 30, 2006. These financial statements reflect the changes in the resources available to pay benefits to retirees and beneficiaries, at the end of the year reported.

(2) Notes to the Financial Statements. The Notes to the Financial Statements provide additional information that is essential for a full understanding of the data provided in the financial statements. The information in the Notes to the Financial Statements is described as follows:

- Note A provides a summary of significant accounting policies, including the basis of accounting, capital assets and equipment used in operations, operating lease, GASB 40 Disclosures, methods used to value investments, summaries of investment vendors and other significant accounting policies or explanations.

- Note B provides information about litigation.

- Note C describes the debt obligation of the PERS-DCRP. The INTERCAP implementation loan for the PERS-DCRP is to be paid back over fifteen years. For the fiscal year ended June 30, 2006, the MPORS Defined Benefit fund received a $2,000 inter-entity loan from Department of Administration's (DOA) General fund. This loan was paid in full on August 8, 2006.

- Note D describes the plans' membership and descriptions of the plans administered by the Public Employees' Retirement Board. Summaries of benefits and contribution information are also provided.

(3) Required Supplementary Information. The required supplementary information consists of the schedules of funding progress and required contributions and related notes concerning actuarial information of the defined benefit pension plans administered by the PERB.

Financial Analysis of the Systems – Defined Benefit Plans

Investments

The State of Montana Board of Investments (BOI), as authorized by state law, invests the defined benefit plans' assets in investment pools. Each plan owns an equity position in the pools and receives proportionate investment income from the pool in accordance with respective ownership. The investment pools are: Montana Short Term Investment Pool, Montana Domestic Equity Pool, Retirement Fund Bond Pool, Montana International Pool and Montana Private Equity Pool. Each plan's allocated share of the investment in the pools is shown in the Statement of Fiduciary Net Assets of the plan. Investment gains and losses are reported in the Statement of Changes in Fiduciary Net Assets.

Defined Benefit Plans Total Investments

At June 30, 2006, the PERB's defined benefit plans held total investments of $4.1 billion, an increase of $303 million from fiscal year 2005 investment totals. On the next page are the schedules of Net Assets and Changes in Net Assets for the defined benefit plans.

Analysis of Individual Systems

PERS-DBRP and Education

The PERS-DBRP provides retirement, disability, and death benefits for covered employees of the State, local governments and certain employees of the university systems and school districts. Member and employer contributions and earnings on investments fund the benefits of the plan. The PERS-DBRP and the Education Fund have been combined in these comparisons. The PERS-DBRP net assets held in trust for benefits at June 30, 2006 amounted to $3.5 billion, an increase of $278 million (8.6 percent) from $3.2 billion at June 30, 2005.

Additions to the PERS-DBRP net assets held in trust for benefits include employer, member, and state contributions and investment income. For the fiscal year ended June 30, contributions increased to $155.1 million in fiscal year 2006 from $127.8 million in fiscal year 2005, an increase of $27.3 million (21.4 percent). Contributions increased due to increased salaries being reported to PERS. The plan recognized net investment income of $293.7 million for the fiscal year ended June 30, 2006 compared with net investment income of $245.0 million for the fiscal year ended June 30, 2005. The increase in investment income is due to greater investment returns.

Deductions from the PERS-DBRP net assets held in trust for benefits primarily include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2006, benefits amounted to $153.9 million, an increase of $11.0 million (7.8 percent) from fiscal year 2005. The increase in benefit payments was due to the increase in benefit recipients and the increase in the average recipient's benefit due to guaranteed annual benefit adjustment (GABA). For fiscal year 2006, refunds/distributions amounted to $13.3 million, a decrease of $356 thousand (2.6 percent) from fiscal year 2005. The decrease in refunds/distributions was due to a decrease in number of refunds and the average amount of distributions. For fiscal year 2006, the costs of administering the plan's benefits amounted to $2.9 million, an increase of $317 thousand (12.4 percent) from

Fiduciary Net Assets - Defined Benefit Plans

As of June 30, 2006 *- and comparative totals for June 30, 2005*

(dollars in thousands)

	PERS		JRS		HPORS		SRS	
	2006	2005	2006	2005	2006	2005	2006	2005
Assets:								
Cash and Receivables	102,576	69,284	1,627	1,399	2,320	2,191	5,820	3,953
Securities Lending Collateral	67,426	140,880	1,044	2,191	1,760	3,779	3,268	6,858
Investments	3,419,270	3,174,677	51,067	47,140	86,474	81,601	159,936	147,565
Property and Equipment		1						
Intangible Assets	103	319	1	3	1	3	2	4
Total Assets	3,589,375	3,385,161	53,739	50,733	90,555	87,574	169,026	158,380
Liabilities:								
Securities Lending Collateral	67,426	140,880	1,044	2,191	1,760	3,779	3,268	6,858
Other Payables	966	862	7	7	27	28	89	52
Total Liabilities	68,392	141,742	1,051	2,198	1,787	3,807	3,357	6,910
Total Net Assets	3,520,983	3,243,419	52,688	48,535	88,768	83,767	165,669	151,470

Changes In Fiduciary Net Assets - Defined Benefit Plans

For the year ended June 30, 2006 *- and comparative totals for June 30, 2005*

(dollars in thousands)

	PERS		JRS		HPORS		SRS	
	2006	2005	2006	2005	2006	2005	2006	2005
Additions:								
Contributions	155,161	127,861	1,562	1,574	4,033	4,855	7,245	5,801
Investment Income (Loss)	293,679	244,976	4,344	3,640	7,453	6,353	13,566	11,381
Total Additions	448,840	372,837	5,906	5,214	11,486	11,208	20,811	17,182
Deductions:								
Benefits	153,886	142,789	1,743	1,624	6,365	5,790	6,152	5,527
Refunds/Distributions	13,322	13,678			90	230	383	634
Administrative Expenses	2,886	2,569	12	9	31	29	77	57
Miscellaneous Expenses	1,248	1,073						
Total Deductions	171,342	160,109	1,755	1,633	6,486	6,049	6,612	6,218
Incr/(Decr) in Net Assets	277,498	212,728	4,151	3,581	5,000	5,159	14,199	10,964
Prior Period Adjustments	65	13		-1				1

fiscal year 2005. The increase in administrative expenses for the fiscal year 2006 was mainly due to personal services and computer processing costs.

An actuarial valuation of the PERS-DBRP assets and benefit obligations is usually performed every two years. An additional valuation was performed in 2005. At June 30, 2006, the date of the most recent actuarial valuation, the funded status of the plan increased to 88 percent from 85 percent at June 30, 2005. The PERS-DBRP actuarial value of assets is less than actuarial liabilities by $460.2 million at June 30, 2006, compared with $540.9 million at June 30, 2005. The increase in funded status as of the last actuarial valuation is a result of investment returns greater than the actuarial assumption and the $25 million lump sum received from the

GWPORS		MPORS		FURS		VFCA		TOTAL	
2006	2005	2006	2005	2006	2005	2006	2005	2006	2005
2,907	3,415	12,958	10,396	12,185	9,760	1,921	2,086	142,314	102,484
1,158	2,296	3,349	7,083	3,189	6,725	464	922	81,658	170,734
56,614	48,458	165,079	151,478	157,225	144,044	21,563	19,552	4,117,228	3,814,515
									1
2	4	1	4	1	4	3	5	114	346
60,681	54,173	181,387	168,961	172,600	160,533	23,951	22,565	4,341,314	4,088,080
1,158	2,296	3,349	7,083	3,189	6,725	464	922	81,658	170,734
58	51	66	64	56	53	46	43	1,315	1,160
1,216	2,347	3,415	7,147	3,245	6,778	510	965	82,973	171,894
59,465	51,826	177,972	161,814	169,355	153,755	23,441	21,600	4,258,341	3,916,186

GWPORS		MPORS		FURS		VFCA		TOTAL	
2006	2005	2006	2005	2006	2005	2006	2005	2006	2005
5,418	5,077	14,766	13,920	13,333	12,008	1,610	1,527	203,128	172,623
4,594	3,696	14,091	11,708	13,409	11,141	1,853	1,550	352,989	294,445
10,012	8,773	28,857	25,628	26,742	23,149	3,463	3,077	556,117	467,068
1,835	1,539	12,032	11,363	11,040	10,386	1,564	1,517	194,617	180,535
490	613	599	798	46	101			14,930	16,054
49	42	68	65	58	53	48	47	3,229	2,871
						11	11	1,259	1,084
2,374	2,194	12,699	12,226	11,144	10,540	1,623	1,575	214,035	200,544
7,638	6,580	16,158	13,402	15,598	12,609	1,840	1,502	342,082	266,524
	1		1		1		3	65	19

State of Montana General Fund for the purpose of reducing the unfunded liability.

JRS

The JRS provides retirement, disability and death benefits for all Montana judges of the district courts, justices of the Supreme Court and the Chief Water Judge. Member and employer contributions and earnings on investments fund the benefits of the plan. The JRS net assets held in trust for benefits at June 30, 2006 amounted to $52.7 million, an increase of $4.2 million (8.6 percent) from $48.5 million at June 30, 2005.

Additions to the JRS net assets held in trust for benefits include member and employer contributions and investment income. For the fiscal year ended June 30, 2006, contributions amounted to $1.56 million a decrease of $12 thousand (0.7 percent) from fiscal year 2005. Contributions decreased due to fewer members contributing to the plan and experience of the system. The plan recognized net investment income of $4.3 million for the fiscal year ended June 30, 2006 compared with net investment income of $3.6 million for the fiscal year ended June 30, 2005. The increase in investment income is due to greater investment returns.

Deductions from the JRS net assets held in trust for benefits mainly include retirement benefits and administrative expenses. For fiscal year 2006, benefits amounted to $1.7 million an increase of $119 thousand (7.3 percent) from fiscal year 2005. The increase for benefits was due to an increase in the average recipient's benefit (GABA), and benefits commencing for new retirees. For fiscal year 2006, administrative expenses amounted to $12 thousand, an increase of $3 thousand (30.7 percent) from fiscal year 2005. The increase in administrative expenses for the fiscal year 2006 was mostly due to increased costs to administer the plan.

An actuarial valuation of the JRS assets and benefit obligations is usually performed every two years. An additional valuation was performed in 2005. At June 30, 2006, the date of the most recent actuarial valuation, the funded status of the plan increased to 139 percent from 138 percent at June 30, 2005. The JRS actuarial assets were more than actuarial liabilities by $15.0 million at June 30, 2006, compared with $13.0 million actuarial surplus at June 30, 2005. The increase in funded status as of the last actuarial valuation is due to investment returns greater than the actuarial assumption.

HPORS

The HPORS provides retirement, disability and death benefits for members of the Montana Highway Patrol. Member and employer contributions, registration fees and earnings on investments fund the benefits of the plan. The HPORS net assets held in trust for benefits at June 30, 2006 amounted to $88.8 million, an increase of $5 million (6.0 percent) from $83.8 million at June 30, 2005.

Additions to the HPORS net assets held in trust for benefits include employer and member contributions, registration fees and investment income. For the fiscal year ended June 30, contributions decreased to $4.0 million in fiscal year 2006 from $4.8 million in fiscal year 2005, a decrease of $822 thousand (16.9 percent). Contributions decreased due to the number of participating members contributing to the plan decreased. The plan recognized net investment income of $7.5 million for the fiscal year ended June 30, 2006 compared with net investment income of $6.4 million for the fiscal year ended June 30, 2005. The increase in investment income is due to greater investment returns.

Deductions from the HPORS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2006, benefits amounted to $6.4 million, an increase of $575 thousand (9.9 percent) from fiscal year 2005. The increase in benefit payments was due to the increase in benefit recipients and increases in the average recipient's benefit, (GABA). For fiscal year 2006 refunds/ distributions amounted to $90 thousand, a decrease of $140 thousand (61.0 percent) from fiscal year 2005. The decrease in refunds/distributions was due to fewer distributions and smaller amounts distributed. For fiscal year 2006, administrative expenses were $31 thousand, an increase of $2 thousand (5.8 percent) from fiscal year 2005. The increase in administrative expenses is due to increased costs to administer the plan.

An actuarial valuation of the HPORS assets and benefit obligations is usually performed every two years. An additional valuation was performed in 2005. At June 30, 2006, the date of the most recent actuarial valuation, the funded status of the plan increased to 78 percent from 73 percent at June 30, 2005. The HPORS actuarial assets were less than actuarial liabilities by $25.0 million at June 30, 2006, compared with $31.0 million at June 30, 2005. The increase in funded status as of the last actuarial valuation is due to investment returns greater than the actuarial assumption.

SRS

The SRS provides retirement, disability and death benefits for all Department of Justice criminal investigators hired after July 1, 1993, detention officers and all Montana sheriffs. Member and employer contributions and earnings on investments fund the benefits of the plan. The SRS net assets held in trust for benefits at June 30, 2006 amounted to $165.7 million, an increase of $14.2 million (9.4 percent) from $151.5 million at June 30, 2005.

Additions to the SRS net assets held in trust for benefits include member and employer contributions and investment income. For the fiscal year ended June 30, contributions increased to $7.2 million in fiscal year 2006 from $5.8 million in fiscal year 2005, for an increase of $1.4 million (24.9 percent). Contributions increased because the number of participating members contributing to the plan increased as a result of the detention officers having the option to elect either PERS or SRS, and an increase in the total compensation reported for active members. The plan recognized net investment income of $13.6 million for the fiscal year ended June 30, 2006 compared with net investment income of $11.4 million for the fiscal year ended June 30, 2005. The increase in investment income is due to greater investment returns.

Deductions from the SRS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2006, benefits amounted to $6.2 million, an increase of $625 thousand (11.3 percent) from fiscal year 2005. The increase in benefit payments was due to an increase in benefit recipients and an increase in the average recipient's benefit (GABA). For fiscal year 2006, refunds/ distributions amounted to $383 thousand, a decrease of $251 thousand (39.7 percent) from fiscal year 2005. The decrease in refunds/distributions was due to smaller balances being refunded to an increased number of members caused resulting from detention officers election. For fiscal year 2006, administrative expenses increased $21 thousand (35.9 percent) from fiscal year 2005. The increase is due to increased costs to administer the plan.

An actuarial valuation of the SRS assets and benefit obligations is usually performed every two years. An additional valuation was performed in 2005. At June 30, 2006, the date of the most recent actuarial valuation, the funded status of the plan increased to 95 percent from 93 percent at June 30, 2005. The SRS actuarial assets were less than actuarial liabilities by $8.8 million at June 30, 2006, compared with $10.9 million at June 30, 2005. The increase in funded status as of the last actuarial valuation is due to investment returns greater than the actuarial assumptions and experience of the plan.

GWPORS

The GWPORS provides retirement, disability and death benefits for game wardens, warden supervisory personnel and state peace officers. Member and employer contributions and earnings on investments fund the benefits of the plan. The GWPORS net assets held in trust for benefits at June 30, 2006 amounted to $59.5 million, an increase of $7.6 million (14.7 percent) from $51.8 million at June 30, 2005.

Additions to the GWPORS net assets held in trust for benefits include member and employer contributions and investment income. For the fiscal year ended June 30, contributions increased to $5.4 million in fiscal year 2006 from $5.1 million in fiscal year 2005, for an increase of $341 thousand (6.7 percent). Contributions increased because the number of members contributing to the plan increased. The plan recognized net investment income of $4.6 million for the fiscal year ended June 30, 2006 compared with net investment income of $3.7 million for the fiscal year ended June 30, 2005. The increase in investment income is due to greater investment returns.

Deductions from the GWPORS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2006, benefits amounted to $1.8 million, an increase of $296 thousand (19.2 percent) from fiscal year 2005. The increase in benefit payments was due to the increase in benefit recipients and the increase in the average recipient's benefit (GABA). For fiscal year 2006, refunds/distributions amounted to $490 thousand, a decrease of $123 thousand (20.1 percent) from fiscal year 2005. The decrease in refunds/distributions was due to refunds for smaller amounts and fewer refunds. For fiscal year 2006, administrative expenses amounted to $49.0 thousand, an increase of $6.6 thousand (15.8 percent) from fiscal year 2005. The increase in administrative expenses in fiscal year 2006 is due to increased costs to administer the plan.

An actuarial valuation of the GWPORS assets and benefit obligations is usually performed every two years. An additional valuation was performed in 2005. At June 30, 2006, the date of the most recent actuarial valuation, the funded status of the plan increased slightly to 92 percent from 90 percent at June 30, 2005. The GWPORS actuarial assets were less than actuarial liabilities by $5.4 million at June 30, 2006, compared with $5.5 million at June 30, 2005. The change in unfunded liability as of the last actuarial valuation is due to investment returns greater than the actuarial assumption and the experience of the plan.

MPORS

The MPORS provides retirement, disability and death benefits for municipal police officers employed by first- and second-class cities and other cities that adopt the plan. MPORS also has an option for members to participate in a Deferred Retirement Option Plan (DROP). Member, employer and state *contributions and earnings on investments fund the benefits of the plan.* The MPORS net assets held in trust for benefits at June 30, 2006 amounted to $177.9 million, an increase of $16.1 million (10.0 percent) from $161.8 million at June 30, 2005.

Additions to the MPORS net assets held in trust for benefits include employer, member, and state contributions and investment income. For the fiscal year ended June 30, contributions increased to $14.8 million in fiscal year 2006 from $13.9 million in fiscal year 2005, for an increase of $846 thousand (6.1 percent). Contributions increased because the total compensation reported for active members increased and membership increased. The plan recognized net investment income of $14.1 million for the fiscal year ended June 30, 2006 compared with net investment income of $11.7 million for fiscal year ended June 30, 2005. The increase in investment income is due to greater investment returns.

Deductions from the MPORS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2006, benefits amounted to $12.0 million, an increase of $669 thousand (5.9 percent) from fiscal year 2005. The increase in benefit payments was due to the increase in benefit recipients and the increase in the average recipient's benefit (GABA). For fiscal year 2006, refunds/distributions amounted to $599 thousand, a decrease of $199 thousand (24.9 percent) from fiscal year 2005. The decrease in refunds/distributions was due to fewer refunds and smaller DROP refunds. For fiscal year 2006, administrative expenses were $68 thousand, an increase of $3 thousand (5.0 percent) from fiscal year 2005. The increase in administrative expenses in fiscal year 2006 is due to increased costs to administer the plan.

An actuarial valuation of the MPORS assets and benefit obligations is usually performed every two years. An additional valuation was performed in 2005. At June 30, 2006, the date of the most recent actuarial valuation, the funded status of the plan increased to 60 percent from 58 percent at June 30, 2005. The MPORS actuarial assets were less than actuarial liabilities by $115.2 million at June 30, 2006, compared with $116.9 million actuarial liabilities at June 30, 2005. The increase in funded status as of the last actuarial valuation is due to investment returns greater than the actuarial assumption and experience of the plan.

FURS

The FURS provides retirement, disability and death benefits for firefighters employed by first- and second-class cities and other cities that adopt the plan, and firefighters hired by the Montana Air National Guard on or after October 1, 2001. Member, employer, and state contributions and earnings on investments fund the benefits of the plan. The FURS net assets held in trust for benefits at June 30, 2006 amounted to $169.4 million, an increase of $15.6 million (10.1 percent) from $153.8 million at June 30, 2005.

Additions to the FURS net assets held in trust for benefits include employer, member, and state contributions and investment income. For the fiscal year ended June 30, contributions increased to $13.3 million in fiscal year 2006 from $12.0 million in fiscal year 2005, an increase of $1.3 million (11.0 percent). Contributions increased because the number of members contributing to the plan increased and the total compensation reported for active members increased. The plan recognized net investment income of $13.4 million for the fiscal year ended June 30, 2006 compared with net investment income of $11.1 million for the fiscal year ended June 30, 2005. The increase in investment income is due to greater investment returns.

Deductions from the FURS net assets held in trust for benefits mainly include retirement benefits, refunds/distributions and administrative expenses. For fiscal year 2006, benefits amounted to $11.0 million, an increase of $654 thousand (6.3 percent) from fiscal year 2005. The increase in benefit payments was due to the increase in benefit recipients and the increase in the average recipient's benefit (GABA). For fiscal year 2006, refunds/distributions amounted to $46 thousand, a decrease of $55 thousand (54.8 percent) from fiscal year 2005. The decrease in refunds/distributions was due to refunds of accounts with smaller balances. For fiscal year 2006, administrative expenses were $58 thousand, an increase of $5 thousand (9 percent). The increase in administrative expenses is due to increased costs to administer the plan.

An actuarial valuation of the FURS assets and benefit obligations is usually performed every two years. At June 30, 2006, the date of the most recent actuarial valuation, the funded status of the plan increased to 65 percent from 64 percent at June 30, 2005. The FURS actuarial assets were less than actuarial liabilities by $88.2 million at June 30, 2006, compared with $86.8 million actuarial liability at June 30, 2005. The increase in funded status as of the last actuarial valuation is due to investment returns greater than the actuarial assumption.

VFCA

The VFCA provides retirement, disability and death benefits for volunteer firefighters who are members of eligible volunteer fire companies in unincorporated areas. State contributions and earnings on investments fund the benefits of the plan. The VFCA net assets held in trust for benefits at June 30, 2006 amounted to $23.4 million, an increase of $1.8 million (8.5 percent) from $21.6 million at June 30, 2005.

Additions to the VFCA net assets held in trust for benefits include state contributions and investment income. For the fiscal year ended June 30, contributions increased to 1.6 million in fiscal year 2006 from $1.5 million in fiscal year 2005, an increase of $83 thousand (5.5 percent). Contributions increased because there was an increase in the fire insurance premium taxes collected. The plan recognized net investment income of $1.9 million for the fiscal year ended June 30, 2006 compared with net investment income of $1.6 million for the fiscal year ended June 30, 2005. The increase in investment income is due to greater investment returns.

Deductions from the VFCA net assets held in trust for benefits mainly include retirement benefits, administrative expenses and supplemental insurance payments. For fiscal year 2006, benefits amounted to $1.6 million, an increase of $47 thousand (3.1 percent) from fiscal year 2005. For fiscal year 2006, administrative expenses amounted to $48 thousand, an increase of $1 thousand (1 percent) from fiscal year 2005. The increase in administrative expenses was due to increased costs to administer the plan. For fiscal year 2006, supplemental insurance payments amounted to $11.4 thousand, an increase of $300 from fiscal year 2005.

An actuarial valuation of the VFCA assets and benefit obligations is usually performed every two years. At June30, 2006, the date of the most recent actuarial valuation, the funded status of the plan increased to 73 percent from 69 percent at June 30, 2005. The VFCA actuarial assets were less than actuarial liabilities by $8.6 million at June 30, 2006, compared with $9.5 million at June 30, 2005.

The increase in funded status as of the last actuarial valuation is due to investment returns greater than the actuarial assumption and experience of the plan.

Actuarial Valuations and Funding Progress

An actuarial valuation of each of the PERB's defined benefit plans is usually performed every two years. An additional valuation was performed in 2005. At the date of the most recent actuarial valuation, June 30, 2006, the funded status of each of the plans is shown in the Schedule of Funding Progress on page 76.

The PERB funding objective is to meet long-term benefit obligations through investment income and contributions. Accordingly, the collection of employer and member contributions, and the income from investments provide the reserves needed to finance future retirement benefits. Since investment earnings are critical to the defined benefit plans' funding, the market decline and associated investment losses in fiscal year 2000 through fiscal year 2003 have deteriorated the plans' funding. However, in more recent years there have been better returns and an increased funding status has occurred in all Defined Benefit plans over the previous valuation. The investment losses reduced the assets available to pay previously incurred benefit obligations. Public pension plans are considered actuarially sound if the unfunded accrued actuarial liability amortization period is less than 30 years. Montana's constitution requires that public retirement plans be funded on an actuarially sound basis.

The PERB has been concerned with the funding of three of the eight defined benefit retirement plans administered. The three plans are the PERS-Defined Benefit Retirement Plan (PERS-DBRP), the Game Wardens' and Peace Officers' Retirement System (GWPORS) and the Sheriffs' Retirement System (SRS). The PERS and GWPORS statutory contribution rates are able to pay the normal cost of the plan, but are insufficient to pay off unfunded liability. The SRS statutory contribution rate is not sufficient to pay the normal cost of the plan or the unfunded liability. Based on the PERB's June 30, 2006 Actuarial Valuations the unfunded liability in these three plans will not be amortized in 30 years. As of June 30, 2006, the estimated shortfalls in statutory contributions rates were 1.01% in PERS-DBRP, 0.04% in GWPORS, and 1.84% in SRS.

Funding ratios range from a high of 139.42 percent (JRS) to a low of 60.43 percent (MPORS). The Schedule of Funding Progress on pages 76 and 77 show the June 30, 2006 funding ratios compared with the ratios at June 30, 2005, June 30, 2004 and June 30, 2002. The table also shows the amount by which actuarial assets exceeded or fell short of actuarial liabilities. The funding ratio increase is a result of the overall investment performance this past year and the actual experience of the plans. The actuary performs a smoothing of investment gains/losses over a period of four years. At June 30, 2006, the actuarial value of assets was less than the market value of assets by $71 million. At June 30, 2005, the actuarial value of assets was less than the market value of assets by $76 million.

Defined Contribution Plans

The MPERA administers two defined contribution plans: The Public Employees' Retirement System-Defined Contribution Retirement Plan (PERS-DCRP) and the Deferred Compensation (457) Plan. The schedules of

Fiduciary Net Assets - Defined Contribution Plans

As of June 30, 2006 *- and comparative totals for June 30, 2005*

(dollars in thousands)

	PERS-DCRP		457-PLAN		TOTAL	
	2006	2005	2006	2005	2006	2005
Assets:						
Cash and Receivables	1,119	605	350	303	1,469	908
Securities Lending Collateral	14		5		19	
Investments	30,934	24,948	247,944	239,143	278,878	264,091
Intangible Assets	2	4	105	145	107	149
Total Assets	32,069	25,557	248,404	239,591	280,473	265,148
Liabilities:						
Securities Lending Collateral	14		5		19	
Other Payables	1,435	1,448	172	186	1,607	1,634
Total Liabilities	1,449	1,448	177	186	1,626	1,634
Total Net Assets	30,620	24,109	248,227	239,405	278,847	263,514

Changes In Fiduciary Net Assets - Defined Contribution Plans

For the year ended June 30, 2006 *- and comparative totals for June 30, 2005*

(dollars in thousands)

	PERS-DCRP		457-PLAN		TOTAL	
	2006	2005	2006	2005	2006	2005
Additions:						
Contributions	6,506	5,411	17,251	15,723	23,757	21,134
Investment Income (Loss)	2,098	1,768	3,618	15,267	5,716	17,035
Total Additions	8,604	7,179	20,869	30,990	29,473	38,169
Deductions:						
Refunds/Distributions	1,570	1,873	11,443	15,591	13,013	17,464
Administrative Expenses	227	231	204	289	431	520
Miscellaneous Expenses	295	256	737	698	1,032	954
Total Deductions	2,092	2,360	12,384	16,578	14,476	18,938
Incr/(Decr) in Net Assets	6,512	4,819	8,485	14,412	14,997	19,231
Prior Period Adjustments		-8	336	246	336	238

Net Assets and Changes in Net Assets for the two defined contribution plans are above.

PERS-DCRP

The PERS-DCRP is established under Section 401(a) of the Internal Revenue Code. This plan provides retirement, disability and death benefits for plan members. This plan was available to all active PERS members effective July 1, 2002. All new hires to PERS have a 12-month window to file an irrevocable election to join the plan. The plan member and employer contributions and earnings on investments fund the benefits of the plan.

The PERB has received a long-term INTERCAP loan through the Montana Department of Administration from the BOI to fund the plan start-up and implementation costs. The loan was renegotiated in 2005 and the term extended to 2018. As of June 30, 2006, the loan balance is $1.38 million, which is reported in the financial statements as a long-term payable of $1.36 million plus a current payable of $20 thousand.

The plan net assets held in trust for benefits at June 30, 2006 amounted to $30.6 million, an increase of $6.5 million (27.0 percent) from $24.1 million at June 30, 2005.

Additions to the Defined Contribution Retirement Plan net assets held in trust for benefits include contributions and investment income. Contributions increased $1.1 million (20.2 percent) from $5.4 million in fiscal year 2005 to $6.5 million in fiscal year 2006. Contributions increased because of the number of members contributing to the plan increased. The plan recognized net investment income of $2.1 million in fiscal year 2006, up from $1.8 million in fiscal year 2005. The increase in investment income is due to greater investment returns.

Deductions from the Defined Contribution Retirement Plan net assets mainly include member refunds/distributions, administrative expenses and miscellaneous expenses. Refunds/distributions decreased from $1.9 million in fiscal year 2005 to $1.6 million in fiscal year 2006. The $303 thousand decrease in refunds/distributions from 2005 to 2006 was due to fewer defined contribution members taking a distribution immediately after electing the plan and smaller distributions. The costs of administering the plan decreased from $231 thousand in fiscal year 2005 to $227 thousand in fiscal year 2006, a decrease of $4 thousand (1.7 percent) from fiscal year 2005. The decrease in administrative costs was due to vacancy savings resulting from staff turnover. Miscellaneous expenses increased from $256.0 thousand in fiscal year 2005 to $295 thousand in fiscal year 2006, an increase of $39 thousand (15.3 percent) from fiscal year 2005. The increase in miscellaneous expenses was due to increased membership.

Deferred Compensation (457) Plan

The deferred compensation plan is established under Section 457 of the Internal Revenue Code. This plan is a voluntary supplemental retirement savings plan for those who choose to participate. The deferred compensation plan is funded by contributions and by investment earnings. The plan's net assets held in trust for benefits at June 30, 2006 amounted to $248.2 million, an increase of $8.8 million (3.7 percent) from $239.4 million at June 30, 2005.

Additions to the deferred compensation plan net assets held in trust for benefits include contributions and investment income. For fiscal year 2006, contributions increased from those of fiscal year 2005 from $15.7 million to $17.3 million, an increase of $1.6 million (9.7 percent). Contributions increased because of the number of members participating in the plan increased due to new employers joining the plan. The plan recognized net investment income of $3.6 million for fiscal year 2006 compared with net investment income of $15.2 million for fiscal year 2005.

Deductions from the deferred compensation plan net assets mainly include member and beneficiary refunds/distributions, administrative expenses and miscellaneous expenses. For fiscal year 2006, refunds/distributions amounted to $11.4 million, a decrease of $4.1 million (26.6 percent) from $15.6 million at June 30, 2005. The costs of administering the plan decreased from $289 thousand in fiscal year 2005 to $204 thousand in fiscal year 2006, a decrease of $85 thousand (29.5 percent) from fiscal year 2005. The decrease in administrative costs was due to less time being spent on development and maintenance of the 457 web payroll reporting. Miscellaneous expenses increased from $698 thousand in fiscal year 2005 to $737 thousand in fiscal year 2006, an increase of $39 thousand (5.6 percent) from fiscal year 2005. The increase in miscellaneous expense was due to the increased membership.

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Public Employees' Retirement Board

A Component Unit of the State of Montana

Statement of Fiduciary Net Assets - Pension Trust Funds

as of June 30, 2006

	PERS-DBRP	JRS	HPORS	SRS	GWPORS	MPORS
Assets						
Cash and Short-term Investments	$ 93,688,932	1,520,236	2,138,719	5,289,414	2,790,734	4,338,910
Securities Lending Collateral (Note A5)	67,425,935	1,043,832	1,759,894	3,267,725	1,158,265	3,349,214
Receivables						
Interest	7,173,427	106,701	180,781	333,304	115,918	342,415
Accounts Receivable	1,223,678			197,356		94,752
Due from Other Funds	323,838					
Due from Primary Government	28,811					8,181,861
Due from Component Unit	1,995					
Notes Receivable	135,357					
Total Receivables	8,887,106	106,701	180,781	530,660	115,918	8,619,028
Investments, at fair value (Note A5)						
Montana Domestic Equity Pool (MDEP)	1,586,747,062	23,744,351	40,231,879	74,632,967	26,704,722	76,683,078
Retirement Fund Bond Pool (RFBP)	932,047,876	14,685,077	24,889,288	45,822,462	15,805,769	46,943,773
Montana International Pool (MTIP)	630,135,329	9,364,981	15,794,686	29,262,553	10,518,496	30,633,241
Montana Private Equity Pool (MPEP)	203,406,134	3,047,260	5,178,135	9,507,757	3,329,864	10,088,571
Montana Real Estate Pool (MTRP)	15,200,000	225,000	380,000	710,000	255,000	730,000
Real Estate Investments	8,636,356					
Mortgages & Commercial Loans						
net of Accumulated Mortgage Discount	43,096,807					
Defined Contributions Fixed Investments						
Defined Contributions Variable Investments						
Deferred Compensation Life Insurance						
Total Investments	3,419,269,564	51,066,669	86,473,988	159,935,739	56,613,851	165,078,663
Capital Assets						
Property and Equipment, at cost,						
net of Accumulated Depreciation (Note A2)	513					
Intangible Assets, at cost,						
net of Amortization Expense (Note A2)	103,058	728	912	1,505	1,534	1,430
Total Capital Assets	103,571	728	912	1,505	1,534	1,430
Total Assets	3,589,375,108	53,738,166	90,554,294	169,025,043	60,680,302	181,387,245
Liabilities						
Securities Lending Collateral Liability	67,425,935	1,043,832	1,759,894	3,267,725	1,158,265	3,349,214
Accounts Payable	502,593	232	787	18,412	13,939	307
Due to Other Funds	94,227	7,059	25,877	70,397	43,632	62,748
Due to Primary Government	50,135					2,000
Due to Component Unit						
Advances from Primary Government (Note C)						
Deferred Revenue	70,942			14	136	570
Compensated Absences	248,600					35
Total Liabilities	68,392,432	1,051,123	1,786,558	3,356,548	1,215,972	3,414,874
Net Assets Held in Trust for Pension Benefits (see schedule of funding progress, page A-76.)	$ 3,520,982,676	52,687,043	88,767,736	165,668,495	59,464,330	177,972,371

The notes to the financial statements are an integral part of this statement.

Defined Benefit Pension Plans			Defined Contribution Plans			
FURS	VFCA	Total Defined Benefit Pension Plans	PERS-DCRP	457 Plan	Total Defined Contribution Plans	Total Pension Trust Funds 2006
4,247,446	1,875,296	115,889,687	1,024,331	350,271	1,374,602	117,264,289
3,188,555	463,503	81,656,923	14,329	5,310	19,639	81,676,562
325,820	45,253	8,623,619				8,623,619
78,747		1,594,533	8	7	15	1,594,548
		323,838	94,227		94,227	418,065
7,532,591		15,743,263				15,743,263
		1,995				1,995
		135,357				135,357
7,937,158	45,253	26,422,605	94,235	7	94,242	26,516,847
73,144,442	9,871,678	1,911,760,179				1,911,760,179
44,649,947	6,232,966	1,131,077,158				1,131,077,158
29,143,147	4,023,023	758,875,456				758,875,456
9,587,346	1,340,772	245,485,839				245,485,839
700,000	95,000	18,295,000				18,295,000
		8,636,356				8,636,356
		43,096,807				43,096,807
			1,832,487	143,870,263	145,702,750	145,702,750
			29,101,644	104,061,001	133,162,645	133,162,645
				12,316	12,316	12,316
157,224,882	21,563,439	4,117,226,795	30,934,131	247,943,580	278,877,711	4,396,104,506
		513				513
1,221	3,410	113,798	2,215	104,720	106,935	220,733
1,221	3,410	114,311	2,215	104,720	106,935	221,246
172,599,262	23,950,901	4,341,310,321	32,069,241	248,403,888	280,473,129	4,621,783,450
3,188,555	463,503	81,656,923	14,329	5,310	19,639	81,676,562
232		536,502	7,797	155,692	163,489	699,991
52,257	46,360	402,557	10,752	4,756	15,508	418,065
		52,135	21,308	899	22,207	74,342
			24,248		24,248	24,248
			1,360,195		1,360,195	1,360,195
3,806		75,468				75,468
		248,635	10,344	10,878	21,222	269,857
3,244,850	509,863	82,972,220	1,448,973	177,535	1,626,508	84,598,728
169,354,412	23,441,038	4,258,338,101	30,620,268	248,226,353	278,846,621	4,537,184,722

Public Employees' Retirement Board

A Component Unit of the State of Montana

Statement of Changes in Fiduciary Net Assets - Pension Trust Funds
for the year ended June 30, 2006

	PERS-DBRP	JRS	HPORS	SRS	GWPORS	MPORS
Additions						
Contributions (Note D)						
Employer	$ 63,445,414	1,229,014	2,905,165	3,523,607	2,391,091	4,035,331
Plan Member	66,002,308	333,319	847,311	3,682,968	3,007,242	2,545,437
Membership Fees	83					
Interest Reserve Buyback	143,047		3,372	38,445	19,761	3,227
Retirement Incentive Program	123,784					
Registration Fee Collections			277,178			
Miscellaneous Revenue	25,003,605			26		7
State Contributions	442,994					8,181,861
Nonvested Member Forfeitures						
Total Contributions	155,161,235	1,562,333	4,033,026	7,245,046	5,418,094	14,765,863
Investments (Note A5)						
Net Appreciation (Depreciation)						
in Fair Value of Investments	185,484,598	2,816,662	4,300,075	9,021,235	3,243,729	9,752,251
Interest	98,921,274	1,386,960	2,913,412	4,104,926	1,201,444	3,891,789
Dividends	14,161,359	211,305	361,462	661,262	223,072	678,147
Investment Expense	(5,008,119)	(72,823)	(125,327)	(227,403)	(76,494)	(237,074)
Net Investment Income	293,559,112	4,342,104	7,449,622	13,560,020	4,591,751	14,085,113
Securities Lending Income						
Securities Lending Income	5,130,656	79,790	136,753	249,384	86,460	259,165
Securities Lending Rebate and Fees	(5,011,163)	(77,965)	(133,615)	(243,680)	(84,521)	(253,236)
Net Securities Lending Income	119,493	1,825	3,138	5,704	1,939	5,929
Total Net Investment Income	293,678,605	4,343,929	7,452,760	13,565,724	4,593,690	14,091,042
Total Additions	448,839,840	5,906,262	11,485,786	20,810,770	10,011,784	28,856,905
Deductions (Note D)						
Benefits	153,885,649	1,742,859	6,365,115	6,151,890	1,834,767	12,031,585
Refunds/Distributions	12,753,802		89,223	365,372	476,629	550,830
Refunds to Other Plans	568,003		416	17,214	13,423	48,394
Transfers to DCRP	1,064,447					
Transfers to ORP	183,135					
Supplemental Insurance Payments						
Administrative Expenses	2,886,404	11,767	30,668	77,470	48,616	68,276
Miscellaneous Expenses						
Total Deductions	171,341,440	1,754,626	6,485,422	6,611,946	2,373,435	12,699,085
Net Increase (Decrease)	277,498,400	4,151,636	5,000,364	14,198,824	7,638,349	16,157,820
Net Assets Held in Trust for Pension Benefits						
Beginning of Year	3,243,418,873	48,535,407	83,767,372	151,469,671	51,825,981	161,814,551
Prior Period Adjustment	65,403					
End of Year	$ 3,520,982,676	52,687,043	88,767,736	165,668,495	59,464,330	177,972,371

The notes to the financial statements are an integral part of this statement.

Defined Benefit Pension Plans			Defined Contribution Plans			
FURS	VFCA	Total Defined Benefit Pension Plans	PERS-DCRP	457 Plan	Total Defined Contribution Plans	Total Pension Trust Funds 2006
3,328,408		80,858,030	2,319,167	52,457	2,371,624	83,229,654
2,470,766		78,889,351	3,699,360	16,990,026	20,689,386	99,578,737
		83				83
1,406		209,258				209,258
		123,784				123,784
		277,178				277,178
9		25,003,647	223,324	208,964	432,288	25,435,935
7,532,591	1,610,462	17,767,908				17,767,908
			263,685		263,685	263,685
13,333,180	1,610,462	203,129,239	6,505,536	17,251,447	23,756,983	226,886,222
9,351,521	1,263,347	225,233,418	991,131	(5,336,756)	(4,345,625)	220,887,793
3,631,704	534,281	116,585,790	1,106,594	9,428,347	10,534,941	127,120,731
645,789	86,065	17,028,461				17,028,461
(225,582)	(31,538)	(6,004,360)		(473,422)	(473,422)	(6,477,782)
13,403,432	1,852,155	352,843,309	2,097,725	3,618,169	5,715,894	358,559,203
246,550	34,374	6,223,132	503	223	726	6,223,858
(240,911)	(33,591)	(6,078,682)	(501)	(222)	(723)	(6,079,405)
5,639	783	144,450	2	1	3	144,453
13,409,071	1,852,938	352,987,759	2,097,727	3,618,170	5,715,897	358,703,656
26,742,251	3,463,400	556,116,998	8,603,263	20,869,617	29,472,880	585,589,878
11,039,519	1,563,795	194,615,179				194,615,179
45,619		14,281,475	1,570,066	11,443,043	13,013,109	27,294,584
		647,450				647,450
		1,064,447				1,064,447
		183,135				183,135
	11,400	11,400				11,400
57,783	47,529	3,228,513	227,170	203,727	430,897	3,659,410
			295,105	737,382	1,032,487	1,032,487
11,142,921	1,622,724	214,031,599	2,092,341	12,384,152	14,476,493	228,508,092
15,599,330	1,840,676	342,085,399	6,510,922	8,485,465	14,996,387	357,081,786
153,755,082	21,600,362	3,916,187,299	24,109,346	239,405,278	263,514,624	4,179,701,923
		65,403		335,610	335,610	401,013
169,354,412	23,441,038	4,258,338,101	30,620,268	248,226,353	278,846,621	4,537,184,722

Public Employees' Retirement Board

A Component Unit of the State of Montana

Notes to the Financial Statements

for the Fiscal Year Ended June 30, 2006

The Public Employees' Retirement Board (PERB) administers ten retirement plans and the related member education funds. The retirement plans are eight defined benefit plans and two defined contribution plans. The *defined benefit* retirement plans are the Public Employees' Retirement System (PERS-DBRP), Judges' Retirement System (JRS), Highway Patrol Officers' Retirement System (HPORS), Sheriffs' Retirement System (SRS), Game Wardens' and Peace Officers' Retirement System (GWPORS), Municipal Police Officers' Retirement System (MPORS), Firefighters' Unified Retirement System (FURS), and the Volunteer Firefighters' Compensation Act (VFCA). The *defined contribution* retirement plans are the Public Employees' Retirement System (PERS-DCRP) and the Deferred Compensation (IRC §457) Plan. The PERS-DCRP was implemented July 1, 2002. All PERS new hires after July 1, 2002 have a twelve-month window to file an election. The Deferred Compensation Plan is available to employees of the state and university system, and to local political subdivisions that contract for the plan.

PERS members are provided member education as a tool to help them decide between participation in the Defined Benefit Retirement Plan (PERS-DBRP) or the Defined Contribution Retirement Plan (PERS-DCRP). If members are employees of the university system they have a third choice, the Optional Retirement Program (ORP). The plan choice is a one-time irrevocable election. Further education is provided for the members who choose the PERS-DCRP, including information on investment choices.

The assets of each plan are maintained separately, including member education funds, and may be used only for the payment of benefits to the members and administrative expenses of the appropriate plan, in accordance with the terms of each plan as prescribed in Title 19, of the Montana Code Annotated (MCA). The financial statements are presented by combining the PERS-DBRP and the DBRP Education Fund and by combining the PERS-DCRP, the DCRP Education Fund and the DCRP Disability Fund. A presentation of each individual fund is shown at the end of the financial section.

A. Summary of Significant Accounting Policies

1. Basis of Accounting

The PERB is a discretely presented component unit Pension Trust Fund of the State of Montana financial reporting entity. The Montana Public Employee Retirement Administration (MPERA), staff of the PERB, prepares the accounting records and financial statements for the fiduciary/pension trust funds using the accrual basis of accounting. For the pension trust funds, member contributions are recognized in the period in which contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Revenues are recognized in the accounting period in which they are earned and become measurable. Benefits and refunds/distributions are recognized in the accounting period in which they are due and payable. Expenses are recognized in the period incurred. Administrative expenses are financed through investment earnings on the pension trust fund for the defined benefit plans. Interfund receivables and payables exist at year-end because all defined benefit administrative expenses are accounted for within PERS-DBRP and then allocated to the other defined benefit plans at year-end.

Adjustments to the fiscal year 2006 financial statements consist of a prior period adjustment to the PERS-DBRP plan for prior years employer reporting errors. A prior period adjustment to the 457 plan include an entry made to balance the fixed annuity based on the reconciliation process.

The PERS requested an inter-entity loan in the amount of $2,000 from the Department of Administration general fund to the Municipal Police Officers Retirement System (MPORS) fund at the end of fiscal year 2006. This loan was due to a check that was returned for insufficient funds. This check was processed before June 30, 2006 and was returned the first week of July. Department of Administration (DOA) treasury reversed the cash entries as fiscal year 2006, putting the MPORS fund in the situation of negative cash at June 30, 2006. This loan was repaid on August 8, 2006.

House Bill No. 1: "Appropriate Funds for Schools, TRS, & PERS" was passed in the Legislative Special Session of December 2005. This Bill saw the appropriation of $25 million from the State of Montana general fund to the PERS pension trust fund for unfunded liability. This amount is shown as a miscellaneous revenue item in the financial statements.

Participants of the PERS-DCRP are charged, on a quarterly basis, a flat fee plus a basis point fee on their account balance. The flat fee covers the recordkeeping provided by Great West Retirement Services (Great West). The basis point fee is remitted to the PERB to cover the PERB's administrative expenses of the plan. The fees returned to the PERB are recorded as *Miscellaneous Revenue* in the financial statements.

Participants of the deferred compensation (457) plan are charged fees, quarterly, based on individual account balances. The record keeper, Great West, withholds fees and after payment of the Great West's contractual expenses, the excess fees are remitted to the PERB. The excess fees, recorded as *Miscellaneous Revenue* in the financial statements, are used to pay the PERB's related administrative expenses.

2. Capital Assets and Equipment Used in Operations

Assets under $5,000 are expensed in the year purchased. Assets valued at $5,000 or more, are recorded at cost less straight-line depreciation over the estimated useful life of five to ten years. Equipment for the MPERA consists of a microfiche reader/printer and a server. Capital assets include the web-based employer reporting software and the MPERA Website.

The accumulated depreciation on the web based reporting system is $1,206,664 as of June 30, 2006. The carrying value as of June 30, 2006 is $66,318. For the 457 web based employer-reporting system the accumulated depreciation as of June 30, 2006 is $89,263 and the carrying value is $98,423. The accumulated depreciation on the MPERA website as of June 30, 2006 is $18,492 and the carrying value is $49,786. A new server was purchased in September 2005. The accumulated depreciation of the server as of June 30, 2006 is $1,659 and the carrying value is $6,305.

3. Operating Lease

Operating leases are rental agreements where the payments are chargeable as rent and recorded as administrative expenses. The MPERA entered into a 10-year lease for office space in November 2003, at the location of 100 North Park. The lease is payable monthly and includes inflationary adjustments over the period of the lease.

4. GASB 40 Disclosures

Effective June 30, 2005, the State of Montana Board of Investments (BOI), Department of Commerce, implemented the provisions of the Governmental Accounting Standards Board (GASB) Statement No. 40 – Deposit and Investment Risk Disclosures. The definition of the investment risk disclosures are as follows:

Credit Risk is defined as the risk that an issuer or other counterparty to an investment will not fulfill its obligation.

Custodial Credit Risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party.

Concentration of Credit Risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. Investments issued or explicitly guaranteed by the U.S. government are excluded from the concentration of credit risk requirement.

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

Foreign Currency Risk is the risk that changes in exchange rates will adversely affect the fair value of an investment.

If applicable, investment risks are disclosed within the investment summaries that begin on the next page.

5. Method Used to Value Investments

According to Article VIII, Section 13 of the Montana Constitution and 19-2-504, MCA, the BOI has a fiduciary responsibility for investing the defined benefit retirement plan assets on behalf of the defined benefit plans. Investments are determined in accordance with the statutorily and constitutionally mandated "prudent expert principle." Pursuant to Article VIII, Section 15 of the Montana Constitution and 19-2-502, MCA, the PERB has a fiduciary responsibility for the administration of the pension trust funds. Investments are reported at fair value. As of June 30, 2006, there were six major diversified pools, Montana Short Term Investment Pool (STIP), Montana Domestic Equity Pool (MDEP), Retirement Funds Bond Pool (RFBP), Montana International Pool (MTIP), Montana Private Equity Pool (MPEP) and Montana Real Estate Investment Pool (MTRP).

The PERS-DCRP and the deferred compensation plan's fixed assets were invested and managed on behalf of the plans by Pacific Investment Management Company (PIMCO)/State Street Bank Kansas City (SSKC). The third party record keeper, Great West Retirement Services, tracks and reports the daily trading and valuations of all investment options including the assets held by the individual mutual fund companies. In addition to the laws cited above, the PERS-DCRP is also governed by 19-3-2122, MCA and there are separate investment policies for the 401(a) defined contribution and 457 deferred compensation plans. The investment policies are reviewed on an annual basis and the investment options are reviewed at least annually by an independent third party consultant and investment analyst. In the review, each investment alternative is compared to its peers and the appropriate benchmark and compared against the relevant Investment Policy Statement. In addition, each investment alternative is reviewed for other indicators including, but not limited to, style drift, duplication, fund manager or other organizational changes. Investment alternatives that are determined to have a substandard performance rating or other negative indicators may be recommended for probation or termination. Investments are reported at fair value as of June 30, 2006.

The following are the PERB summaries of the BOI's fiscal year end statements, the PIMCO/SSKC contract and a statement about the variable investments.

STIP portfolio may include asset-backed securities, commercial paper, corporate and government securities, repurchase agreements and variable-rate (floating-rate) instruments. These securities provide a diversified portfolio earning a competitive total rate of return. Funds may be invested for relatively short periods. State agencies are legally required to invest in STIP and the PERB elects to have all STIP income automatically reinvested. Investments are reported at fair value based on market prices supplied to the BOI by the BOI's custodial bank. The unit value is fixed at $1.00. A purchased unit earns income on the purchase date and ceases to earn income on the day before the unit is sold. STIP income reflects the monthly earnings of the STIP portfolio and is distributed on the first calendar day of the month, with the exception of the June distribution. Income for June is distributed on the last calendar day of the month. Administrative expenses incurred by the BOI are charged daily to STIP based on their expenses applicable to STIP. As of June 30, 2006, the carrying and fair value of the underlying securities on loan, categorized as U.S. Government indirect-backed bonds, for the Short Term Investment Pool was $35,271,669 and $35,219,601 respectively. STIP did not participate in any securities lending transactions in fiscal year 2005. STIP is considered an external investment pool per the Governmental Accounting Standards Board (GASB) Statement No. 31 and is classified as a "2a7-like" pool. STIP is not registered with the Securities and Exchange Commission (SEC) but does operate in a manner consistent with SEC rules. *Credit Risk* is that the issuer of a STIP security may default in making timely principal and interest payments. Obligations of the U.S. government or

Security Investment Type (in thousands)	Fair Value 2006	Credit Quality Rating
Commercial Paper	$ 1,421,009	A1
Corporate Fixed	293,960	A1+
Corporate Variable-Rate	224,992	A1+
US Gov. Indirect-Backed	248,885	A1+
Total Investments	$ 2,188,846	A1+
Securities Lending Collateral Investment Pool	$ 36,072	NR

obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. STIP securities have credit risk as measured by major credit rating services. STIP investments are required to have the highest rating in the short-term category by at least one Nationally Recognized Statistical Rating Organization (NRSRO). The table above displays all STIP investments for the State of Montana. The PERB portion of STIP is 4.0 percent. Investments are categorized to disclose credit rate risk as of June 30, 2006. If a security investment type is unrated, the quality type is indicated by NR (not rated). As an external investment pool, STIP has not been rated by the NRSRO. For *Custodial Credit Risk* as of June 30, 2006, all the investments were registered in the nominee name for the BOI and held in the possession of the BOI's custodial bank, State Street Bank (SSB). According to the STIP Investment Policy "repurchase agreements require electronic delivery of U.S. Government Treasury collateral, priced at 102 percent market value, to the designated State of Montana Federal Reserve Bank account." *Concentration of Credit Risk* as of June 30, 2006, the STIP had concentration of credit risk exposure to the Federal Home Loan Bank of 6.59%. As of June 30, 2005, there were no single issuer investments that exceeded 5% of the STIP portfolio. The STIP Investment Policy Statement does not specifically address concentration of credit risk. The policy does provide for "minimum 3 percent or $15 million, whichever is higher, to be invested in Repurchase Agreements." *Interest Rate Risk* disclosures are not required for "2a7-like" pools. Corporate asset-backed securities are based on cash flows from principal and interest payments on underlying auto loan receivables, credit card receivables and other assets. These securities, while sensitive to prepayments due to interest rate changes, have less credit risk than securities not backed by pledged assets. While variable-rate (floating-rate) securities have credit risk identical to similar fixed-rate securities, their interest rate risk is more sensitive to interest rate changes. However, their fair value may be less volatile than fixed-rate securities because their value will usually remain at or near par as a result of their interest rates being periodically reset to maintain a current market yield. STIP security transactions are recorded as of the trade date rather than the settlement date. Because of this generally accepted practice, the STIP portfolio at June 30 may include receivables from brokers for securities sold, but not delivered, and payables to brokers for securities purchased, but not received. There are no legal risks that the BOI is aware of regarding any STIP investments.

MDEP portfolio may include common stock, equity index, preferred stock, convertible equity securities, American Depositary Receipts and equity derivatives. The MDEP was established in April 2003. Effective May 1, 2003, the retirement funds transferred all the Barclays Global Investors (BGI) S&P 500 Equity

Index Fund A and the Dimensional Fund Advisors (DFA) Small Cap Subtrust investments totaling $740 million, at cost, from the All Other Funds portfolio to the new pool. The pensions also exchanged their investment in the Montana Stock Pool (MTCP) for units in the new MDEP. In July 2003, the BOI closed the STIP account and a Stock Performance Index Futures Fund (SPIFF) account was opened to securitize MDEP cash by investing in an equity derivative. The value of MDEP units purchased and sold by participants is the result of an asset allocation decision and pool participants' cash needs. Investments are presented at fair value. Unit values are calculated weekly and at the close of the last business day of the month. Equity investments, on valuation date, are stated at the closing price of the security's primary exchange. Depending on stock market conditions and the investment officer's decision, MDEP participants may then buy or sell units on the first calendar day of each month. MDEP security transactions are recorded as of trade date rather than settlement date. Because of this generally accepted practice, the MDEP portfolio at June 30 may include receivables from brokers for securities sold but not delivered, and payables to brokers for securities purchased but not received. Administrative expenses incurred by the BOI are charged daily to MDEP based on the board's expenses applicable to MDEP. The PERB portion of MDEP is 60.64 percent. For *Custodial Credit Risk* as of June 30, 2006, all the MDEP securities were registered in the nominee name for the BOI and held in the possession of the BOI's custodial bank, State Street Bank. The BGI S&P 500 Equity Index Fund A, S&P 400 MidCap Equity Index fund, DFA Small Cap Subtrust, Goldman Sachs and Western Asset (WAMCO) commingled funds are registered in the name of the Montana BOI. *Concentration of Credit Risk* as of June 30, 2006 - there were no single issuer investments that exceeded 5% of the MDEP portfolio.

On October 11, 2002, the BOI received a summons and complaint regarding the bankruptcy of Owens-Corning. The company seeks a determination that the dividend payments paid from October 1996 through July 2000 represent "fraudulent transfers under Chapter 11 Bankruptcy provisions and applicable state law, and are, therefore, voidable". The complaint states the BOI was the "recipient of dividends in the amount of $357,099 for the relevant period". The BOI has prepared a response to the complaint. As of September 22, 2006, this matter is still pending.

In July 2005, the BOI agreed to lease a Portfolio Order Management System (POMS) from Bloomberg Financial Services. This electronic securities trading system reduces trading time and paperwork, increases trading and accounting accuracy, and provides certain controls not previously available. Electronic trading began with the internally-managed component of the MDEP in August 2005. Implementation of electronic trading for the STIP and the other fixed income portfolios, as managed by the BOI staff, was completed in fiscal year 2006.

RFBP portfolio includes corporate securities, foreign government bonds, U.S. government direct-backed, U.S. government indirect-backed and cash equivalents. RFBP investments are presented at fair value. Fair values are determined, primarily, by reference to fair market prices supplied to the BOI by its custodial bank, State Street Bank. Premiums and discounts are amortized/accreted using the straight-line or scientific method to the call, average life or maturity date of the securities. Unit values are calculated weekly and at month end, based on portfolio pricing, to allow for participant transactions to occur as determined by the BOI's staff. The June 30, 2006 unit value of $99.81 decreased from the June 30, 2005 unit value of $105.31. The yield on longer term bonds increased during the fiscal year, which has the effect of decreasing bond prices and the pool unit value. The pension funds were rebalanced in fiscal year 2006 to adjust the portfolios toward the stated equity/fixed income allocation. RFBP security transactions are recorded as of the trade date rather than the settlement date. Because of this generally accepted practice, the RFBP portfolio at June 30 may include receivables from brokers for securities sold, but not delivered, and payables to brokers for securities purchased, but not received. Accumulated income is distributed monthly on the first calendar day of the month. Realized portfolio gains/losses are distributed at least annually. Administrative expenses incurred by the BOI are charged daily to RFBP based on applicable BOI expenses. *Credit Risk* is that the issuer of a fixed income security may default in making timely principal and interest payments. RFBP fixed income investments are required to be rated an investment grade as defined by Moody's or by S&P rating services. Refer to the table at the top of the next column. Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. For *Custodial Credit Risk* as of June 30, 2006, all the investments were registered

Security Investment Type (in thousands)	Fair Value 2006	Credit Quality Rating	Effective Duration
Corporate Bonds (Rated)	$ 930,859	A	5.20
Corporate Bonds (Unrated)	13,929	NR	3.81
Foreign Government Bonds	4,850	BBB	5.83
U.S. Government Direct-Backed	55,508	AAA	6.87
U.S. Government Indirect-Backed	722,334	AAA	4.73
State Street Repurchase Agrmt	448	AA-	NA
Short Term Investment Pool	109,117	NR	NA
Total Fixed Income Investments	$ 1,837,045	AA-	5.05
Securities Lending Collateral Investment Pool	$ 84,097	NR	NA

in the nominee name for the BOI and held in the possession of the BOI's custodial bank, State Street Bank. The State Street repurchase agreement was purchased in the State of Montana BOI name. As of June 30, 2006 the RFBP had *Concentration of Credit Risk* exposure to the Federal Home Loan Mortgage Corp of 5.50%. According to the RFBP Investment Policy, "with the exception of the U.S. government indirect-backed securities, additional RFBP portfolio purchases will not be made if the credit risk exceeds 2 percent of the portfolio at the time of purchase". The RFBP investment policy does not formally address *Interest Rate Risk*. In accordance with GASB Statement No. 40, the BOI has selected the effective duration method to disclose interest rate risk. The table above displays RFBP investments for the State of Montana. The PERB portion of RFBP is 50.74 percent. If a bond investment type is unrated, the quality type is indicated by NR (not rated). Both the credit quality ratings and duration have been calculated excluding cash equivalents. If duration has not been calculated, duration is indicated by NA (not applicable).

Corporate asset-backed securities are based on cash flows from principal and interest payments on underlying auto loan receivables, credit card receivables and other assets. These securities, while sensitive to prepayments due to interest rate changes, have less credit risk than securities not backed by pledged assets. The RFBP portfolio holds REMICs (Real Estate Mortgage Investment Conduits) totaling $387,052 in amortized cost as of June 30, 2006. These securities are based on separate or combined cash flows from principal and interest payments on underlying mortgages. The interest-only (IO) are more sensitive to prepayments by mortgagees resulting from interest rate changes than other REMIC securities. The IO securities purchased in August and September 1992 carry an amortized cost of $3 as of June 30, 2006.

As of June 30, 2005, Delta Airlines Corp. presented a higher credit risk to the BOI. The RFBP holds $3 million par 10.0% Delta Airlines Corp. bond maturing June 5, 2013, a $1.971 million par 10.0% Delta Airlines Corp. bond maturing June 5, 2011 and a $6 million par 10.14% Delta Airlines Corp. bond maturing August 14, 2012. Due to a weak credit outlook and potential bankruptcy, the BOI stopped the interest income accruals after the December 2004 and February 2005 pay dates. Although the interest accruals were stopped, the BOI received the interest due in June 2005 and August 2005. The combined book value of these securities was $11 million as of June 30, 2005. Due to the company's filing for Chapter 11 bankruptcy protection on September 14, 2005, the book values were reduced to $1.5 million, $985,500 and $3 million, respectively. On March 20, 2006, the BOI sold these securities and recorded a combined gain of $892,680.

As of June 30, 2006, Northwest Airlines Inc. presented a higher credit risk to the BOI. The RFBP held a $5.7 million par 4.64% Northwest Airlines Inc. real estate backed bond maturing July 7, 2010. The 4.64% bond maturing July 7, 2010 is secured by Northwest Airlines Inc.'s corporate headquarters' building and land. As of June 30, 2005 the RFBP held a $9.9 million par 6.81% Northwest Airlines Inc. bond maturing February 1, 2020 and a $7.8 million par 7.935% Northwest Airlines Inc. MBIA Insurance Corp. insured bond maturing April 1, 2019. The combined book value of these securities was $17.2 million as of June 30, 2005. On September 14, 2005, the company filed for Chapter 11 bankruptcy protection. Due to this action, the BOI stopped the interest income accruals for the 6.81% bond maturing February 1, 2020 after the August 2005 pay date. This issue was sold on September 20, 2005 generating a loss of $642,183. The sale included accrued interest from August 1, 2005 to September 20, 2005. Since the 7.935% bond maturing April 1, 2019 is insured by MBIA Insurance Corp. to support the payment of any interest due and outstanding principal balance, the BOI did not stop the interest income accrual or reduce book value. On January 11, 2006 Northwest Airlines Inc. called the 7.935% bond maturing April 1, 2019 at par and included accrued interest from October 1, 2005 to January 11, 2006. The BOI recorded a gain of $132,710 on this transaction.

As of June 30, 2006, Burlington Industries, Inc. presented legal and higher credit risks to the BOI. The BOI owns a Burlington Industries, Inc., $6 million par, 7.25% bond maturing September 15, 2005. In September 2000, the company announced a reduction of stockholders' equity. Due to an increasing senior bank line and declining credit trend, the bond ratings for this issue were downgraded, in May 2001, by the Moody's and Standard & Poor's rating agencies. During fiscal year 2001, the book value of Burlington Industries Inc. was reduced from the August 31, 2000 book value of $5.6 million to $2.4 million. Due to the company's filing for Chapter 11 bankruptcy protection on November 11, 2001, the book value was reduced to $1.2 million. In October 2003, Burlington Industries, Inc. received court approval to sell its assets. Under the company's recovery plan, the BOI received $1.5 million in August 2004 for its unsecured claim. This transaction reduced the book value to $0 and generated a gain of $254,961. In February 2005 and May 2005, the BOI received an additional $208,771 and $194,247 respectively for this unsecured claim. In May 2006, the BOI received an additional payment of $158,278. The BOI is expected to receive the final distribution in September 2006.

The BOI received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, $5 million par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25, 2002 sale of the bond at a price of $94.669 plus accrued interest. Deutsche Bank Securities seeks damages of $538,632 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State debt. The BOI tendered the Pennzoil Quaker State holdings on October 8, 2002 at a price of $113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, the BOI received $5.7 million in principal and interest plus $150,000 as a consent fee. As of June 30, 2006, this matter is still pending.

MTIP portfolio includes equities with six externally managed funds at June 30, 2006: Schroder Investment Management NA, Nomura Asset Management, Barclays Global Investors (BGI) Equity Index Fund Europe, Barclays Global Investors (BGI) Passive Pacific Index Strategy, Dimensional Fund Advisors (DFA) International Small Co., and State Street EAFE ISPIFF. In November 2005, the BOI approved the securitization of MTIP cash by investing in an international equity derivative, the State Street EAFE (Europe, Asia, Far East) International Stock Performance Index Futures Fund (ISPIFF). MTIP cash was previously invested in the domestic SPIFF. In December 2005, the BOI terminated Pyrford International, the European external manager. The BOI transferred $1.2 million Pyrford International units held by MTIP at a gain of $39.5 million to the BGI Restructure account. Closure of the BGI Restructure account to the BGI MSCI Europe Index Fund resulted in additional gains of $1.5 million. Because transactions are recorded as of the trade date rather than settlement date, the MTIP portfolio may include receivables from brokers for securities sold, but not deliv-

MTIP Cash by Currency

Cash (in thousands)		Fair Value 2006
Australian Dollar	$	68
Hong Kong Dollar		699
Japanese Yen		1,317
South Korean Won		24
Malaysian Ringgit		9
Philippine Peso		3
Singapore Dollar		1,367
New Taiwan Dollar		168
Total Cash	$	3,655

MTIP Investment by Security Type

Security Investment Type (in thousands)		Fair Value 2006
BGI MSCI Europe Index	$	768,769
BGI MSCI Pacific Index		65,943
BGI Cash and Money Market		-
DFA International Small Co.		93,071
State Stree EAFE ISPIFF		30,496
Schroder Investment Mgmt		139,113
Nomura Asset Management		143,656
Total Investments	$	1,241,048
Securities Lending Collateral Investment Pool	$	31,331

ered, and payables to brokers for securities purchased, but not received. Investments are presented at current U.S. dollar value after conversion from foreign currency by the custodial bank, State Street Bank and Trust. Unit values are calculated weekly and once a month at the close of the last business day of the month, based upon the fair value of the MTIP equity holdings, other assets and liabilities. Based on the BOI Investment Officer's decision, participants are allowed to buy or sell units on the first business day of each month. Realized gains/losses from the sale of securities and related foreign exchange transactions are retained by each fund. MTIP income is distributed at least monthly to the retirement funds, net of external manager fees and administrative expenses, on the first business day of the following month. For *Custodial Credit Risk* as of June 30, 2006, all MTIP securities were registered in the nominee name for the Montana BOI and held in the possession of the BOI's custodial bank, State Street Bank. The BGI MSCI Europe and Pacific Index and the DFA Small Company Portfolio are registered in the name of the Montana BOI. *Foreign Currency Risk* is the risk that changes in exchange rates will adversely affect the fair value of an investment. The MTIP has significant investments in 11 foreign countries. Future economic and political developments in these countries could adversely affect the liquidity or value or both of the securities in which MTIP is invested. The table to the left discloses the investments by currency and investment type in U.S. dollars. The PERB portion of MTIP is 50.77 percent.

MPEP portfolio includes venture capital, leveraged buyout, mezzanine, distressed debt, special situation and secondary investments. The MPEP was established in April 2002 to allow retirement funds the opportunity to participate in the venture capital and leveraged buyout markets and other private equity investments via a diversified pool. Given the complexity and specialization of private equity investment, the BOI contracts with eleven private equity managers. The private equity managers include Adams Street Partners (formerly Brinson Partners); Kohlberg, Kravis, Roberts and Company (KKR); Welsh Carson Anderson and Stowe; Madison Dearborn Partners; Lexington Partners; Oaktree Capital Management; ArcLight Energy Partners; Oak Hill Capital Partners; JLL Partners, Inc.; Odyssey

Investment Partners and Carlyle Partners. Investments are presented at fair value and because no recognized market exists for private equity investment, the investments, on valuation date, are stated at the fair value reported in the most recent external managers' valuation reports. The pool portfolio is priced quarterly. Unit values are calculated at month end and participant transactions will most likely occur on a quarterly basis. Based on the BOI Investment Officer's decision, participants are allowed to buy, reinvest or sell units on the first business day of each month. Administrative expenses incurred by the BOI are charged daily to the MPEP based on the BOI's expenses applicable to MPEP. For *Custodial Credit Risk* as of June 30, 2006, all MPEP investments were recorded in the name of the Montana BOI. The State Street Bank and Trust repurchase agreement for $447,174, as of June 30, 2005 was purchased in the Montana BOI's name. This repurchase agreement was collateralized at $458,263 by a AAA rated Federal Home Loan Mortgage Corporation note maturing February 15, 2006. *Foreign Currency Risk* includes several MPEP investments that represent limited partnership investments in various foreign countries. Per GASB Statement No. 40, no foreign currency risk disclosure is required for these limited partnership investments. Private equity investments are recognized as investments with a higher degree of risk with a higher return potential. *Specific Risk* associated with MPEP is portfolio diversification achieved through multiple partnership relationships and investments diversified by time, financing stage, industry sector, investment size and geographical region. Private equity investments typically have a low correlation relative to other investment asset classes and contribute to the reduction of portfolio risk. The PERB portion of MPEP is 61.25 percent.

In October 2004, the BOI committed $25 million to Inter Mountain Private Equity Partners, LP, a regional venture capital "fund of funds" with Credit Suisse First Boston (CSFB), as the General Partner. This commitment was contingent upon CSFB raising an additional $15 million from other investors in the region. Despite best efforts, the Fund dissolved May 2006 and the Board's commitment was withdrawn. For a private equity commitment the BOI on August 24, 2006 funded the initial capital call in Carlyle Venture Fund III of $4.4 million which included investment and management fees. In July 2006, the staff committed $25 million to JC Flowers Sidecare Fun II, a buyout fund focused on the global financial services industry. On August 14, 2006, the board made the initial investment of $1.8 million. In July 2006, the staff committed $30 million to First Reserve Corp Fund XI, a buyout fund focused on the energy industry. In August 2006, the staff committed $35 million to Lehman Brothers Co-Investment Fund I and $30 million to CCMP Capital Investors Fund II. Both managers invest in mid-market buyout funds.

MTRP was approved by BOI on April 26, 2006, to permit the state's retirement systems to participate in a diversified real estate portfolio. The BOI approved the original MTRP May 1998, to allow retirement and endowment funds the opportunity to participate in the Real Estate Investment Trust (REIT) equity market via a diversified pool. The original was created on July 1, 1998 by a spin-off of the REIT stock investments held in the Montana Stock Pool (MTCP). On March 1, 2001, BOI approved liquidation of the MTRP and all REIT securities were sold. As of June 30, 2001, all accounts related to the original Montana Real Estate Pool reported a zero balance. Investments are presented at fair value. The MTRP will invest with external real estate managers with both open-end and closed-end pooled funds. The MTRP, as an internal investment pool, invests its excess cash in the BOI's STIP. The pension funds sold STIP shares totaling $30 million to fund the MTRP on June 1, 2006. Each pension fund participant was issued units in the new pool at an initial unit value of $100. Unit values are calculated on the close of the last business day of the month. Based on the investment officer's decision, participants may buy or sell units on the first business day of each month. MTRP will not participate in security lending because of the characteristics of the portfolio. At June 30, 2006, no securities were on loan for the MTRP. *Credit Risk*: STIP, as an external investment pool, has not been rated by a Nationally Recognized Statistical Rating Organizations (NRSRO). The six NRSRO's include Standard and Poors (S&P), Moody's, Duff and Phelps, Fitch, IBCA and Thompson's Bank Watch. The *Custodial Credit Risk* as of June 30, 2006 for the MTRP investment in STIP was recorded in the name of the BOI. The *Concentration of Credit Risk* as of June 30, 2006 is MTRP's single investment of the Montana's STIP. *Interest Rate Risk* according to GASB Statement No. 40, "interest rate disclosure are not required for pooled investments if the pool is a 2a-7-like pool". This is the case for the MTRP. *Specific* Risks associated with MTRP are achieved through multiple manager relationships and investments diversified by time, real estate type, real estate size, and geographical region. As of September 22, 2006 BOI has made commitments, but not yet funded, the following real estate managers: AG Core Plus Realty Fund II, Apollo Real Estate Finance Corp., ABR Chesapeake III, and TA Associates Realty Fund VIII. The PERB portion of MTRP, which only is applicable to PERS, is 15.1 percent.

All Other Funds (AOF) Investments are owned by various State of Montana agencies and managed on their behalf by the BOI. The portfolio for the pension plans include real estate, mortgages and other equity. Fair values are determined, primarily, by reference to market prices supplied to the BOI by its custodial bank, State Street Bank and Trust. The real estate investments and residential and multifamily mortgages are valued based on a discounted cash flow. The mortgages receivable funded by the retirement systems consist of residential mortgages. As of June 30, 2006, there were no uncollectible account balances for mortgages. Real estate investments held, in part, for the PERS include buildings at 100 North Park Avenue in Helena, MT; in 2004 a building constructed at 2273 Boot Hill Court in Bozeman, MT; a building at 2401 Colonial Drive in Helena, MT; and property located on California Street in Helena, MT. The BOI also holds the building located at 1712 Ninth Avenue in Helena, MT for the sole benefit of the PERS. *Credit Risk* as of June 30, 2006 the PERB did not hold fixed income investments in the AOF financial statements. The U.S. government securities are guaranteed directly or indirectly by the U.S. government and are not considered to have credit risk and do not require disclosure of credit quality. For Montana mortgages, there is a lien on the real estate property. In the event of default, the property can be sold. *Custodial Credit Risk* as of June 30, 2006 has all other equity, real estate, and mortgage investments registered in the name of the Montana BOI. *Concentration of Credit Risk* is not addressed in the investment policy statements. The single issuer for residential mortgages would be the residential borrower and there are no single issuers that have a principal balance in excess of 5 percent. *Interest Rate Risk* is not formally addressed in the AOF investment policies. In accordance with GASB Statement No. 40, the BOI has selected the effective duration method to disclose interest rate risk.

Securities Lending Collateral, governed under the provisions of state statutes, authorizes the custodial bank, State Street Bank and Trust, to lend the BOI's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. This is accomplished by the BOI via a Securities Lending Authorization Agreement. During the period the securities are on loan, the BOI receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the fair value of the loaned security and maintain collateral equal to 100 percent of the fair value of the loaned security. These percentages for foreign currency is 105 percent of both loaned security and maintaining collateral. The BOI retains all rights and risks of ownership during the loan period. During fiscal year 2006, State Street Bank and Trust loaned, on behalf of the BOI, certain securities held by State Street Bank and Trust, as custodian, and received U.S. dollar and foreign (international invesing) currency cash, U.S. government securities, sovereign debt of foreign countries, and irrevocable bank letters of credit. State Street Bank and Trust does not have the ability to pledge or sell collateral securities unless the borrower defaults. The BOI did not impose any restrictions during fiscal year 2006 on the amount of the loans that State Street Bank and Trust made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal year 2006. Moreover, there were no losses during fiscal year 2006 resulting from a default of the borrowers or State Street Bank and Trust. During fiscal year 2006, the BOI and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the BOI's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the BOI could not determine. At year-end, the BOI has no *Credit Risk* exposure to borrowers because the amounts the BOI owes the borrowers exceed the amounts the borrowers owe the system. For MTCP and MDEP as of June 30, 2006, the carrying and fair values of the underlying securities on loan were $12 million and $12.6 million, respectively. The cash collateral provided for the securities on loan totaled $12.9 million. For RFBP as of June 30, 2006, the carrying and fair values of the underlying securities on loan were $82.1 million and $81.7 million, respectively. The cash collateral provided for the securities on loan totaled $84.1 million in cash and $381,000 in securities collateral. For MTIP as of June 30, 2006, the carrying and fair values of the underlying securities on loan were $31.3 million. The cash collateral provided for the securities on loan totaled $31.3 million.

Fixed Investments are administered through outside vendors Pacific Investment Management Company (PIMCO) and custodial bank State Street Bank Kansas City (SSKC). When participants invest in the fixed investment they are guaranteed a rate of return. The fixed investment employs a synthetic stable value strategy where the investment manager manages a diversified bond portfolio and the third party insurer guarantees the participants principal investments and earnings. The third party insurer resets the rate of return each quarter.

The PERS-DCRP fixed money is invested in a PIMCO mutual fund. The deferred compensation fixed investment is a separately managed fund that is benchmarked against the Lehman Intermediate Government/Credit/Yankee index with a duration not to exceed four years. The minimum average portfolio quality must be an A-rating; the minimum issue quality must be a BB-rating and the minimum commercial paper quality must be A2/P2. The quality ratings applied are the higher of Moody's, Standard & Poor or Fitch. PIMCO has the discretion to invest in a broad array of public and private asset classes and investment vehicles including: money market instruments; U.S. Treasury and Agency notes and bonds; municipal bonds; corporate securities; Yankee and Euro bonds; mortgage-backed securities; mortgage derivatives; asset-backed securities; convertible securities; non-U.S. dollar denominated securities; non-leveraged structured notes; futures; options; swaps; credit default swaps; emerging market securities; and PIMCO pooled funds. All investments, including those with derivative characteristics, are reported at fair value. PIMCO may not invest in: caps and floors; preferred stock; event-linked bonds; and bank loans. *Concentration of Credit Risk* is not addressed in the investment policy. However, principal and rate of return are guaranteed for participants.

Variable Investments are held and managed by a selection of retail and institutional mutual funds, which cover all standard asset classes and categories. The selection of offered mutual funds is designed to provide plan participants with the ability to diversify and meet their individual investment goals and strategies. The PERB, with the advice of the statutorily created Employee Investment Advisory Council and the assistance of an independent contracted third-party consultant and investment analyst, conducts an annual review of the offered mutual funds. The goal of the annual review is to ensure the offered mutual funds meet standards established in the Investment Policy Statement adopted by the PERB. The investment policy states that "Participants make individual investment decisions, subject to the investments offered under the plan and, ultimately, bear the risks and rewards of investment returns." In the annual review, each investment alternative is compared to its peers and the appropriate benchmark. In addition, each investment alternative is reviewed for other indicators including, but not limited to, style drift, duplication, fund manager or other organizational changes. Investment alternatives that are determined to have a sub-standard performance rating or other negative indicators may be recommended for probation or termination. During the annual review, the PERB may decide to retain, replace or place in a watch status, any of the offered mutual funds. *Concentration of Credit Risk* is not addressed in the investment policy and investments in mutual funds are not required to be disclosed.

Investments are reported at fair value as of June 30, 2006. Available mutual funds are listed on pages 67 and 70 or a listing can be obtained by contacting the MPERA.

B. Litigation

Each of the plans administered by the PERB may be involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management and legal counsel, the disposition of those matters will not have a material, adverse affect on any plans' financial position as a whole.

A lawsuit, ***Baumgardner v. PER Board*** (Cause No. ADV-2002-450, First Judicial District), has been filed challenging the constitutionality of that portion of Chapter 149, L. of 2001 which, in the definition of "actuarial equivalent", substituted "the mortality table and interest rate assumptions adopted by the Board" for "the 1971 Group Annuity Mortality Table, with ages set back 4 years and an interest rate of 8% compounded annually". This amendment was effective March 29, 2001. Subsequent to the legislation, effective July 1, 2001, the PERB adopted new actuarial assumptions, including new mortality tables, resulting in new actuarial equivalent option factors. The legal challenge is the use of these new actuarial equivalent option factors in determining the actuarial equivalent benefit payout when a single life benefit is converted to an alternate form of benefit payment. The plaintiff seeks recalculation of benefit payments and attorney's fees. The action was filed by a PERS member, but was certified as a class action lawsuit and could affect other systems where members have the option to choose a benefit payment other than for the member's life only.

Three constitutional claims have been made: 1) that the legislation contained more than one subject matter, not properly reflected in the title; 2) that the legislation was an unconstitutional delegation of legislative authority; and 3) that the legislation constituted an unconstitutional impairment of contract. The District Court dismissed the first claim; found in favor of the plaintiff on the second claim; and has not ruled on the third claim. The Montana Supreme Court (Cause No. 04-861) reversed the District Court's ruling on the second issue, and the case has been returned to the District Court on remittitur. The Plaintiff requested amendments to his complaint alleging two additional claims, violation of equal protection and noncompliance with the Montana Administrative Procedure Act in the adoption of the new option factors. The District Court denied the plaintiff's request to amend his complaint.

An adverse decision would have different actuarial consequences depending on the breadth of the court's ultimate decision. Accurately assessing the chances of ultimately prevailing on the remaining claim is very difficult due to the complexity of the issues presented and the status of the case. This case is expected to be heard in November 2006.

Bean, et al v. Montana and MPERA (Cause No. ADV-2004-707, First Judicial District) challenges the constitutionality of Chapter 290, L. of 2001 which allowed firefighters hired by the Montana Air National Guard on or after October 1, 2001 to join the Firefighters' Unified Retirement System (FURS) rather than the Public Employees' Retirement System (PERS). Plaintiffs, hired before October 1, 2001, claim the law is a violation of equal protection and seek coverage under FURS. A counterclaim seeks proper FURS employee contributions from plaintiffs if they are determined to be covered by FURS. Cross motions for summary judgment were filed, following which District Judge Dorothy McCarter determined that the legislation violates the equal protection clause of the constitution. Pending determination of attorney fees to be awarded, the matter will be appealed to the Montana Supreme Court. If the lower court's decision stands, the PERB will then determine the proper remedy. If the statute is in fact unconstitutional, members hired on or after October 1, 2001 may be moved to PERS. Meanwhile, "new" members remain in FURS and members hired prior to October 1, 2001 remain in PERS. The actuarial impact on the PERS and FURS has not been determined. However, a material actuarial impact of an adverse decision is remote.

Hall v. State of Montana and the Public Employees' Retirement Board (Cause No. 05-124, Montana Supreme Court) was appealed to the Montana Supreme Court from a District Court decision dismissing a FURS equal protection claim on a statute of limitations basis. The Montana Supreme Court upheld the dismissal, but for different reasons. Specifically, the court determined that it is the employer's responsibility to determine the amount of compensation that should be reported to the PERB for each employee. The PERB did not err in receiving contributions and paying retirement benefits based on compensation reported to the PERB by the plaintiffs' employers. No actuarial impact, material or otherwise, resulted from this determination.

Internal Revenue Service Voluntary Correction Program Filing (September 7, 2005). MPERA has identified an employer who has claimed as compensation the amounts paid for group insurance that were not paid by employees through a properly administered IRC Section 125 plan. This procedure was used for the employer's PERS, MPORS, and FURS contributions for a number of years. The identified employer has proposed a self-correction plan for its Section 125 plan which, if acceptable to the IRS and applied to all affected employers, would settle the issue without unanticipated financial consequences to the pension funds. Acceptance is pending.

The PERB filed a Voluntary Correction Program Filing with the IRS, seeking approval of the PERB's related rules and policies, and approval of the PERB's acceptance of the employer's self-correction plan. The IRS has voiced acceptance of the PERB's proposal for all individuals other than highly compensated employees (HCEs). The PERB has acquiesced to correcting the reporting error with respect to the one HCE, and is awaiting IRS approval. Meanwhile, MPERA is working with the Montana Department of Revenue's Local Government auditors to include IRC Section 125 plan issues in that Department's random audits to avoid future issues. Given the IRS's tentative approval of the PERB's VCP, the probability of a net material, adverse affect on any plan's financial position as a whole is remote.

Thane v. Montana Public Employee Retirement Administration. Mr. Thane recently requested that he be permitted to transfer his Teacher's Retirement system (TRS) service into the Public Employees' Retirement System (PERS). Based on 19-3-511(3), MCA, MPERA permits transfer of TRS service to PERS on a month-to-month basis. Therefore, if the member worked nine months in TRS-covered employment over the course of a fiscal year, the member receives nine months service credit in PERS for that time. Mr. Thane believes he should receive 12 months service credit in PERS for each year he worked in a TRS-covered position, regardless the number of months actually worked in that year. If Mr. Thane prevails, he will receive a total of 24 additional months of service credit in PERS at no additional cost. The total increase of all past TRS members who transfer their TRS time to PERS is unknown, but the impact to PERS could be material should Mr. Thane prevail.

C. Debt Obligation

The PERS defined contribution retirement plan has an implementation loan through the Department of Administration, with the BOI. Authorization for the INTERCAP loan was provided by the Legislature, Chapter 471, Laws of 1999. Five draws were taken in the total amount of $1,498,000. Interest repayments began immediately following the draws. Principal repayments began August 15, 2003, the year following the DCRP implementation date. The loan was renegotiated as a single sum in fiscal year 2004 to be repaid over a period of 15 years. The interest rate is variable and changes every February, impacting the interest due on the outstanding principal balance. The financial statements report the long-term payable in Advances from Primary Government for the amount $1,360,195. The additional $20,000 is reported in Due To Primary Government as a current payable.

Debt service requirements (principal and interest) for the defined contribution plan are explained in the chart on the top of the next page.

Schedule of Debt Repayment

INTERCAP Loan

Fiscal Year Ended	Rate*	Principal	Interest	Total
2007	4.75%	$ 20,000	$ 65,320	$ 85,320
2008	4.75%	30,000	64,075	94,075
2009	4.75%	40,000	62,878	102,878
2010	4.75%	50,000	60,686	110,686
2011	4.75%	70,000	58,071	128,071
2012-2018	4.75%	1,170,195	247,636	1,417,831
		$ 1,380,195		$ 1,938,861

* Interest rate is variable. As of June 30, 2006 the interest rate was 4.75 %.

D. Plan Membership, Descriptions and Contribution Information

The plans are established and amended statutorily by the Legislature. In all defined benefit plans (except VFCA), if a member leaves covered employment before retirement, the member contributions plus accrued interest may be refunded to the member. If a member returns to service and repays the withdrawn contributions plus the interest the contributions would have earned had they remained on deposit, membership service is fully restored. Membership of each plan as of June 30, 2006 and June 30 2005 is detailed in the charts below and on the following pages:

PERS-DBRP Membership

	2006	2005		2006	2005
Number of participating employers	524	530			
Active plan members	27,962	28,213	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	14,988	14,579
Vested	2,530	2,418	Disability Retirements	342	338
Non-vested	7,178	8,153	Survivor Benefits	324	303
	9,708	10,571		15,654	15,220

JRS Membership

	2006	2005		2006	2005
Number of participating employers	1	1			
Active plan members	50	50	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	49	47
Vested	3	4	Disability Retirements	-	-
Non-vested	-	-	Survivor Benefits	2	2
	3	4		51	49

HPORS Membership

	2006	2005		2006	2005
Number of participating employers	1	1			
Active plan members	197	201	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	265	258
Vested	13	10	Disability Retirements	7	8
Non-vested	11	9	Survivor Benefits	10	10
	24	19		282	276

SRS Membership

	2006	2005		2006	2005
Number of participating employers	57	56			
Active plan members	1,006	680	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	313	291
Vested	39	42	Disability Retirements	33	34
Non-vested	102	81	Survivor Benefits	15	15
	141	123		361	340

GWPORS Membership

	2006	2005		2006	2005
Number of participating employers	7	8			
Active plan members	793	711	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	102	91
Vested	30	22	Disability Retirements	1	-
Non-vested	81	81	Survivor Benefits	3	3
	111	103		106	94

MPORS Membership

	2006	2005		2006	2005
Number of participating employers	22	22			
Active plan members	617	605	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	538	532
Vested	29	26	Disability Retirements	14	15
Non-vested	40	35	Survivor Benefits	28	28
	69	61		580	575

FURS Membership

	2006	2005		2006	2005
Number of participating employers	17	15			
Active plan members	467	444	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	480	477
Vested	10	13	Disability Retirements	6	3
Non-vested	64	50	Survivor Benefits	23	24
	74	63		509	504

VFCA Membership

	2006	2005		2006	2005
Active plan members	2,733	2,754	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits			Service Retirements	994	959
Vested	687	687	Disability Retirements		
			Survivor Benefits	7	7
				1,001	966

PERS-DCRP Membership

	2006	2005		2006	2005
Number of participating employers	229	230			
Active plan members	1,362	1,136	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Benefit Payments	2	10
Vested	95	61	Disability Payments	-	-
Non-vested	182	93	Survivor Payments	-	3
	277	154		2	13

Deferred Compensation (457) Membership

	2006	2005		2006	2005
Number of participating employers	12	10	Number of participating plan members	7,935	7,759
Number of participating employers that provide contributions on members' behalf	1	1	Number of participating plan members that are actively contributing to their deferred compensation accounts	5,357	5,281

Public Employees' Retirement System-DBRP (PERS-DBRP)

Plan Description: The PERS-Defined Benefit Retirement Plan (DBRP) is a multiple-employer, cost-sharing plan established July 1, 1945, and governed by Title 19, chapters 2 & 3, Montana Code Annotated (MCA). This plan covers the State, local governments and certain employees of the university system and school districts.

All new hires are initially members of the PERS-DBRP. New hires have a 12-month window during which they may choose to remain in the PERS-DBRP or join the PERS-DCRP. Members may not be members of both the *defined contribution* and *defined benefit* retirement plans. The choice is irrevocable. All new hires of the universities also have a third option to join the university system's Optional Retirement Program (ORP). For members that choose to join the PERS-DCRP or the ORP, a percentage of the employer contribution will be used to maintain the funding of the PERS-DBRP.

The PERS-DBRP provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are established by state law and can only be amended by the Legislature. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

PERS-DBRP Summary of Benefits

Member's highest average compensation (HAC)
Highest average compensation during any consecutive 36 months

Eligible for benefit
Service retirement:
- 30 years of membership service, any age;
- Age 60, 5 years of membership service; or
- Age 65, regardless of service

Early retirement, actuarially reduced:
- Age 50, 5 years of membership service; or
- Any age, 25 years of membership service

Vesting 5 years of membership service

Monthly benefit formula
Less than 25 years of membership service: 1.785% of HAC per year of service credit;
25 years of membership service or more: 2% of HAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)
After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of other adjustments to the member's benefit

At June 30, 2006 PERS had 524 participating employers, a decrease of 6 from FY2005. The participating employers consist of:

PERS-DBRP EMPLOYERS

Employers	June 30, 2006	June 30, 2005
State Agencies	36	35
Counties	55	55
Cities and Towns	94	95
Colleges and Universities	5	5
School Districts	233	238
High Schools	6	5
Other Agencies	95	97
Total	524	530

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal year 2006 was 6.9% of PERS-covered payroll. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a request for retirement or refund is processed. Each state agency and university system employer contributed 6.9% of PERS-covered payroll during fiscal year 2006. Participating local governments and school district employers contributed 6.8% of PERS-covered payroll during fiscal year 2006. The State contributed the remaining 0.1% for local governments and school district employers from the state general fund. A percentage of the employers' contributions is used to fund the employee education program. (Reference Schedule of Contribution Rates on page 76).

Plan Membership Elections: MPERA has also included in the financial statements transfers of $1,064,447 to Transfers to DCRP and $183,135 to Transfers to ORP. These transfers reflect the DCRP and ORP contributions of participants that filed elections at or near the June 30 cutoff date but the contributions were moved in early fiscal year 2007.

Effective July 1, 2005, Senate Bill 270 provided membership for county detention officers in the SRS. All detention officers hired after July 1, 2005 will be in the SRS. Existing detention officers may elect to remain in the PERS or elect to become a member of the SRS.

PERS-DBRP Active Membership by Employer Type

Employer Type	June 30, 2006	June 30, 2005
State Agencies	10,607	10,549
Counties	5,225	5,526
Cities	3,061	3,002
Universities	2,615	2,642
High Schools	66	56
School Districts	5,258	5,312
Other Agencies	1,130	1,126
Total	27,962	28,213

Additional Service Purchase: A provision (19-2-706, MCA) related to the Employee Protection Act allows state and university system employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. The total number of participants decreased at the end of fiscal year 2006. This decrease was due to 165 employees under HB490 being removed from the count because the outstanding accounts were paid in full in fiscal year 2006. The remaining employees participating under HB567 increased from 158 in fiscal year 2005 to 165 in fiscal year 2006. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. The retirement incentive contributions received (including interest) during fiscal year 2006 totaled $123,784. The outstanding balance at June 30, 2006, totaled $49,261.

Public Employees' Retirement System-DBRP Education Fund: Education is provided to all members of the PERS regardless of plan choice as governed by section 19-3-112, MCA. The education must be presented with impartial and balanced information about plan choices, investments and retirement planning.

The education program consists of three primary components:

1) initial transfer education - complete as of July 1, 2003.
2) ongoing transfer education - for new hire members after the July 1, 2002 plan start date; and
3) ongoing investment/retirement planning education - for all active members.

The education program was funded by 0.04% of PERS-covered payroll in fiscal year 2006.

Actuarial Status: The statutory funding rate is tested in the valuation to determine if it is sufficient to cover the Normal Cost Rate plus an amortization payment of the Unfunded Actuarial Liability, if any, over no more than 30 years. Based on the current Actuarial Value of Assets and all future experience emerging as assumed, the Unfunded Actuarial Liability will not be amortized over the next 30 years. In general, the deterioration of the funded status is primarily due to the dramatic decline in the domestic equity markets from 2000 through 2002. Based on the actuarial assumptions as of June 30, 2006, an additional funding rate of 1.01% of payroll would be required to fund the current and projected benefits from the DB plan in accordance with GASB standards and state law.

Judges' Retirement System (JRS)

Plan Description: The JRS is a single-employer defined benefit plan established in 1967, and governed by Title 19, chapters 2 & 5 of the MCA. This system provides benefits for all Montana judges of the district courts, justices of the Supreme Court, and the Chief Water Judge. Benefits are established by state law and can only be amended by the Legislature. The JRS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits is on the following page:

JRS Summary of Benefits

Member's current salary[1] or highest average compensation (HAC)[2]
[1]Hired prior to July 1, 1997 and non-GABA - monthly compensation at time of retirement;
[2]Hired after June 30, 1997 or electing GABA - HAC during any consecutive 36 months

Eligibility for benefit
Age 60, 5 years of membership service;
Any age with 5 years of membership service - involuntary termination, actuarially reduced

Vesting 5 years of membership service

Monthly benefit formula
3 1/3% of current salary[1] (non-GABA) OR HAC[2] (GABA) per year of service credit for the first 15 years, plus 1.785% per year for each year after 15 years

Guaranteed Annual Benefit Adjustment (GABA)
Hired after July 1, 1997, or those electing GABA - after the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

Minimum benefit adjustment (non-GABA)
Hired prior to July 1, 1997 - current salary is used in the calculation of the monthly benefit each time the Legislature increases salaries for active judges.

At June 30, 2006 JRS had one participating employer, the same as FY2005. The participating employer consists of:

JRS EMPLOYERS

Employer	June 30, 2006	June 30, 2005
State Agency - Supreme Court	1	1
Total	1	1

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal year 2006 was 7.0% of the member's monthly compensation. Contributions are deducted from each member's salary and remitted by the participating employer. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. As the employer, the State contributed 25.81% of the total JRS-covered payroll to the retirement plan during fiscal year 2006. (Reference Schedule of Contribution Rates on page 76).

JRS Active Membership by Employee Type

Employee Type	June 30, 2006	June 30, 2005
GABA	27	25
Non-GABA	23	25
Total	50	50

Highway Patrol Officers' Retirement System (HPORS)

Plan Description: The HPORS is a single-employer, defined benefit plan established July 1, 1971, and governed by Title 19, chapters 2 & 6 of the MCA. This system provides retirement benefits to all members of the Montana Highway Patrol, including supervisory personnel. Benefits are established by state law and can only be amended by the Legislature. The HPORS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

HPORS Summary of Benefits

Member's highest average compensation (HAC)
Highest average compensation during any consecutive 36 months

Eligibility for benefit
20 years of membership service, regardless of age;

Early Retirement
5 years of membership service, actuarially reduced from age 60

Vesting 5 years of membership service

Monthly benefit formula
2.5% of HAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)
Hired after July 1, 1997, or those electing GABA - after the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

Minimum benefit adjustment (non-GABA)
Hired prior to July 1, 1997 - monthly benefits for non-GABA members are increased each July when they fall below a statutorily guaranteed minimum. Any annual increase is limited to 5% over the current benefit and may not exceed 60% of the current base salary of a probationary officer.

At June 30, 2006 HPORS had one participating employer, the same as FY2005. The participating employer consists of:

HPORS EMPLOYERS		
Employer	June 30, 2006	June 30, 2005
State Agency - Dept. of Justice	1	1
Total	1	1

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rates for fiscal year 2006 is 9.05% of the member's total compensation if hired after June 30, 1997 or for members electing GABA and 9.0% for those members hired prior to July 1, 1997 and not electing GABA (all active members hired prior to July 1, 1997 have elected the GABA). Contributions are deducted from each member's salary and remitted by the participating employer. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. As the employer, the State contributed 36.33% of the total HPORS-covered payroll during fiscal year 2006. The first 26.15% is payable from the same source used to pay members' compensation. The remaining amount, equal to 10.18%, is payable from a portion of the fees collected from drivers' license and duplicate drivers' license applications. (Reference Schedule of Contribution Rates on page 76).

HPORS ActiveMembership by Employee Type		
Employee Type	June 30, 2006	June 30, 2005
GABA	197	201
Non-GABA	0	0
Total	197	201

Additional Service Purchase: A provision (19-2-706, MCA) related to the Employee Protection Act allows state and university system employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. No employees have taken advantage of this provision to date.

Supplemental Benefit: Montana highway patrol officers retired prior to July 1, 1991, or their survivors, may be eligible for an annual supplemental lump-sum payment distributed each September. This lump-sum payment is funded by a request of the PERB from the general fund. Many factors must be considered for eligibility, including the number of years the recipient has received a benefit and the recipient's age. The average annual supplemental payment for non-GABA retirees was $3,139 in September 2006.

Sheriffs' Retirement System (SRS)

Plan Description: The SRS is a multiple-employer, cost-sharing defined benefit plan established July 1, 1974, and governed by Title 19, chapters 2 & 7, MCA. This plan provides retirement benefits to all Department of Justice criminal investigators hired after July 1, 1993, and to all Montana sheriffs. Benefits are established by state law and can only be amended by the Legislature. The SRS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service.

Effective July 1, 2005, Senate Bill 370 provided membership for county detention officers in the SRS. All detention officers hired after July 1, 2005 will be in the SRS. Existing detention officers may elect to remain in the PERS or elect to become a member of the SRS. A brief summary of eligibility and benefits follows:

SRS Summary of Benefits

Member's highest average compensation (HAC)
Highest average compensation during any consecutive 36 months

Eligibility for benefit
20 years of membership service, regardless of age;

Early Retirement
Age 50, 5 years of membership service, actuarially reduced

Vesting 5 years of membership service

Monthly benefit formula
2.5% of HAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)
After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit.

At June 30, 2006 SRS had 57 participating employers, one more than FY2005. The participating employers consist of:

SRS EMPLOYERS

Employers	June 30, 2006	June 30, 2005
State Agencies - Dept. of Justice	1	1
Counties	56	55
Total	57	56

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal year 2006 was 9.245% of member's compensation. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Each employer contributed 9.535% of total SRS-covered payroll to the retirement plan during fiscal year 2006. (Reference Schedule of Contribution Rates on page 76).

SRS Active Membership by Employer Type

Employer Type	June 30, 2006	June 30, 2005
Dept of Justice	46	40
Counties	960	640
Total	1,006	680

Additional Service Purchase: A provision (19-2-706, MCA) related to the Employee Protection Act allows state employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. Three employees have taken advantage of this provision to date.

Actuarial Status: The statutory funding rate is tested in the valuation to determine if it is sufficient to cover the Normal Cost Rate plus an amortization payment of the Unfunded Actuarial Liability, if any, over no more than 30 years. Based on the current Actuarial Value of Assets and all future experience emerging as assumed, the Unfunded Actuarial Liability will not be amortized over the next 30 years. In general, the deterioration of the funded status is primarily due to the dramatic decline in the domestic equity markets from 2000 through 2002. Based on the actuarial assumptions as of June 30, 2006, an additional funding rate of 1.84% of payroll would be sufficient to fund the current and projected benefits from the plan in accordance with GASB standards and state law.

Game Wardens' and Peace Officers' Retirement System (GWPORS)

Plan Description: The GWPORS is a multiple-employer, cost-sharing defined benefit plan established in 1963 and is governed by Title 19, chapters 2 & 8, MCA. This system provides retirement benefits to all persons employed as a game warden, warden supervisory personnel, or state peace officer. Benefits are established by state law and can only be amended by the Legislature. The GWPORS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits is on the following page:

GWPORS Summary of Benefits

Member's highest average compensation (HAC)
Highest average compensation during any consecutive 36 months

Eligibility for benefit
Age 50, 20 years of membership service;

Early Retirement
Age 55, 5 years of membership service

Vesting
5 years of membership service

Monthly benefit formula
2.5% of HAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)
After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit.

At June 30, 2006 GWPORS had seven participating employers, one less than FY2005. The participating employers consist of:

GWPORS EMPLOYERS

Employers	June 30, 2006	June 30, 2005
State Agencies	4	5
Colleges and Universities	3	3
Total	7	8

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal year 2006 was 10.56% of member's compensation. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Each state agency and university employer contributed 9.0% of total GWPORS-covered payroll to the retirement plan during fiscal year 2006. (Reference Schedule of Contribution Rates on page 76).

GWPORS Active Membership by Employer

Employer	June 30, 2006	June 30, 2005
Dept of Corrections	576	496
Dept FW&P	94	94
Dept of Justice	0	5
Dept of Livestock	29	28
Dept of Trans.	69	61
Universities	25	27
Total	793	711

Additional Service Purchase: A provision (19-2-706, MCA) related to the Employee Protection Act allows state and university system employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. No employees have taken advantage of this provision to date.

Actuarial Status: The statutory funding rate is tested in the valuation to determine if it is sufficient to cover the Normal Cost Rate plus an amortization payment of the Unfunded Actuarial Liability, if any, over no more than 30 years. Based on the current Actuarial Value of Assets and all future experience emerging as assumed, the Unfunded Actuarial Liability will not be amortized over the next 30 years. In general, the deterioration of the funded status is primarily due to prior investment losses less than the long-term assumed rate of 8% per year. Based on the actuarial assumptions as of June 30, 2006, an additional funding rate of 0.04% of payroll is required to fund the current and projected benefits from the plan in accordance with GASB standards and state law.

Municipal Police Officers' Retirement System (MPORS)

Plan Description: The MPORS is a multiple employer, cost-sharing defined benefit retirement plan established in 1974 and is governed by Title 19, chapters 2 & 9 of the MCA. This plan covers all municipal police officers employed by first- and second-class cities and other cities that adopt the plan. Benefits are established by state law and can only be amended by the Legislature. The MPORS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and compensation. Member rights for death and disability are vested immediately. All other rights are vested after five years of service. A brief summary of eligibility and benefits follows:

MPORS Summary of Benefits

Member's final average compensation (FAC)
Hired prior to July 1, 1977 - average monthly compensation of final year of service;
Hired after June 30, 1977 - final average compensation (FAC) for last consecutive 36 months

Eligibility for benefit
20 years of membership service, regardless of age;

Early Retirement
Age 50, 5 years of membership service

Vesting
5 years of membership service
Monthly benefit formula

2.5% of FAC per year of service credit

Guaranteed Annual Benefit Adjustment (GABA)
After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit.

Minimum benefit adjustment (non-GABA)
If hired before July 1, 1997 and member did not elect GABA, the monthly retirement, disability or survivor's benefit may not be less than ½ the compensation of a newly confirmed officer in the city where the member was last employed.

At June 30, 2006 MPORS had 22 participating employers, the same as in FY2005. The participating employers consist of:

MPORS EMPLOYERS

Employers	June 30, 2006	June 30, 2005
Cities and Towns	22	22
Total	22	22

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. Member contribution rates are dependent upon date of hire as a police officer. For fiscal year 2006, member contributions as a percentage of salary were 5.8% (if employed on or before June 30, 1975); 7.0% (if employed after June 30, 1975 and prior to July 1, 1979); 8.5% (if employed after June 30, 1979 and prior to July 1, 1997); and, 9.0% (if employed on or after July 1, 1997 and for members electing GABA). Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Employer contributions to the retirement plan are 14.41% of total MPORS-covered payroll. The State contributions are requested at the beginning of the fiscal year based on the previous fiscal year compensation and are due no later than November 1. The State's contribution rate for 2006 was 29.37%. (Reference Schedule of Contribution Rates on page 76).

MPORS Active Membership by Employee Type

Employee Type	June 30, 2006	June 30, 2005
GABA	605	593
Non-GABA	12	12
Total	617	605

Deferred Retirement Option Plan (DROP): Beginning July 2002, eligible members of MPORS can participate in the DROP by filing a one-time irrevocable election with the PERB. The DROP is governed by Title 19, chapter 9, part 12, MCA. An eligible member must have completed at least twenty years of membership service. They may elect to participate in the DROP for a minimum of one month and a maximum of 60 months and may participate in the DROP only once. A participant remains a member of the MPORS, but will not receive membership service or service credit in the system for the duration of the member's DROP period. During the participation in the DROP, all mandatory contributions continue to the retirement system. A monthly benefit is calculated based on salary and years of service to the date of the beginning of the DROP period. The monthly benefit is paid into the DROP account until the end of the DROP participation period. At the end of the DROP period, the participant may receive the balance of the DROP account in a lump-sum payment or in a direct rollover to another eligible plan, as allowed by the IRS. If the participant continues employment after the DROP period ends they will again accrue membership service and service credit. The DROP account cannot be distributed until employment is formally terminated. As of June 30, 2006, a total of 54 members have participated in the DROP.

DROP Participation

	6/30/2006	6/30/2005
Participants Beginning of Year	35	32
Participants Added	6	9
Completed DROP	3	6
Participants End of Year	38	35
DROP Distributions	$233,615	$510,348

Firefighters' Unified Retirement System (FURS)

Plan Description: The FURS is a multiple-employer, cost-sharing defined benefit plan established in 1981, and governed by Title 19, chapters 2 & 13, MCA. This system provides retirement benefits to firefighters employed by first- and second-class cities and other cities that adopt the plan, and subject to the Montana Air National Guard (MANG) lawsuit, to firefighters hired by the MANG on or after October 1, 2001. Benefits are established by state law and can only be amended by the Legislature. The FURS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

FURS Summary of Benefits

Member's compensation
Hired prior to July 1, 1981 and not electing GABA – highest monthly compensation (HMC);
Hired after June 30, 1981 and those electing GABA - highest average compensation (HAC) during any consecutive 36 months

Eligibility for benefit
20 years of membership service, regardless of age;

Early Retirement
Age 50, 5 years of membership service

Vesting
5 years of membership service

Monthly benefit formula
Members hired prior to July 1, 1981 and not electing GABA are entitled to the greater of:
2.5% of HAC per year of service, OR
i) if less than 20 years of service,
  2% of HMC for each year of service
ii) if more than 20 years of service,
  50% of the member's HMC plus 2% of the member's HMC for each year of service over 20 years
Members hired after June 30, 1981 and those electing GABA:
2.5% of HAC per year of service

Guaranteed Annual Benefit Adjustment (GABA)
After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit.

Minimum benefit adjustment (non-GABA)
If hired before July 1, 1997 and member did not elect GABA, the monthly retirement, disability or survivor's benefit may not be less than ½ the compensation of a newly confirmed firefighter employed by the city that last employed the member (provided the member has at least ten years of service credit).

At June 30, 2006 FURS had 17 participating employers, two more than FY2005. The participating employers consist of:

FURS EMPLOYERS

Employers	June 30, 2006	June 30, 2005
State Agencies - Dept. of Military Affairs	1	1
Cities and Towns	16	14
Total	17	15

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rates for fiscal year 2006 are 9.5% for members hired prior to July 1, 1997, and 10.7% for members hired after June 30, 1997 and members electing GABA coverage. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Employer contribution rates for fiscal year 2006 were 14.36% of the total FURS-covered payroll. The State contribution was 32.61% of total compensation for all covered firefighters in fiscal year 2006. State contributions are requested at the beginning of each fiscal year based on previous fiscal year salary and are due no later than November 1. (Reference Schedule of Contribution Rates on page 76).

FURS Active Membership by Employee Type

Employee Type	June 30, 2006	June 30, 2005
GABA	460	436
Non-GABA	7	8
Total	467	444

Volunteer Firefighters' Compensation Act (VFCA)

Plan Description: The VFCA is a statewide retirement and disability plan. This compensation plan was established in 1965 and is governed by Title 19, chapter 17, MCA. All members are unpaid volunteers and the State of Montana is the only contributor to the plan. Benefits are established by state law and can only be amended by the Legislature. The VFCA provides pension, disability and survivorship benefits for all volunteer firefighters who are members of qualified volunteer fire companies in unincorporated areas, towns or villages under the laws of the State of Montana. Benefits are based on eligibility and years of service. Member rights are vested after ten years of credited membership service. VFCA also provides limited benefits for injuries incurred in the line of duty.

A member can obtain greater than 20 years of service and when the member retires, a benefit can be drawn on the increased years of service. The maximum years of service allowed is 30 years. For each additional year of service the member's monthly benefit is increased by $7.50.

A member that chooses to retire and draw a pension benefit may return to service with the volunteer fire department without loss of benefits. A returning retired member may not be considered an active member accruing service credit. A brief summary of eligibility and benefits follows:

VFCA Summary of Benefits

Eligibility for benefit
Age 55, 20 years of service credit;
Age 60, 10 years of service credit

Additional Benefit
After April 25, 2005, members that have greater than 20 years of service credit (with a maximum of 30 years) may receive additional benefits (maximum benefit $225).

Vesting 10 years of service credit

Monthly benefit formula
$7.50 per year of service credit, maximum $225 (no more than 30 years).

Contributions: The State is the only contributor to the VFCA. Contributions are 5% of fire insurance premium taxes collected on certain fire risks. The State Auditor makes annual payments from the general fund to the Volunteer Firefighters' Pension Fund from fire insurance premiums. (Reference Schedule of Contribution Rates on page 74).

Group Insurance Payments: Supplemental payments are available to qualified volunteer fire companies that provide additional group medical insurance for their members in case of death or injury incurred while in the line of duty. The payment is made to the volunteer fire companies and is equal to $75 per year for each mobile firefighting unit owned by the volunteer fire company, up to a maximum of two units.

Public Employees' Retirement System-DCRP (PERS-DCRP)

Plan Description: The defined contribution retirement plan (DCRP) is a multiple employer plan established July 1, 2002 and governed by Title 19, chapters 2 & 3, MCA. This plan covers eligible employees of the State, university system, local government and certain employees of the school districts that elect the defined contribution retirement plan. All new hires, initially, are members of the PERS-DBRP. New hires have a 12-month window during which they may choose to transfer to the PERS-DCRP or remain in the PERS-DBRP. The choice is irrevocable. Members may not be members of both the *defined contribution* and *defined benefit* retirement plans. The PERS-DCRP provides retirement, disability and death benefits to plan members and their beneficiaries. Contribution rates can only be amended by the Legislature. Benefits are based on eligibility and account balance.

The PERB has received a long-term INTERCAP loan from the Montana Board of Investments through the Montana Department of Administration to fund the plan start-up/ implementation costs. Authorization for the loan was provided by the Legislature, Chapter 471, Laws of 1999. As of June 30, 2004, all of the draws have been combined into one loan and the maturity date extended to February 2018. The loan is discussed in Note C of the Financial Section.

The investment options offered within the PERS-DCRP are selected by the PERB within the scope of the Investment Policy Statement with the assistance of the statutorily-created Employee Investment Advisory Council and with the advice of a third-party investment analyst. Members of the DCRP decide how to invest their contributions and a portion of their employer's contributions among the offered investment options. The remaining portion of employer's contributions is used to reduce the Plan Choice Rate unfunded actuarial liability to fund the long-term disability benefits to members of the DCRP, and to fund an employee education program. Members are able to invest in any number of the offered investment options and transfer between options. The offered investment options fall into two primary types: (1) the fixed investment option and (2) the variable investment options. The variable investment options include mutual funds and bond funds. All options range from aggressive to conservative. The mutual funds cover all standard asset classes and categoreies. The investment options as of June 30, 2006 are as follows:

PERS-DCRP Investment Options

International Stock Funds
American Funds New Perspective
SSGA International Growth Opportunities
Oakmark International
Barclay's Global Equity Index

Small Company Stock Funds
Brown Capital Small Co Instl
Vanguard Small Cap Index Adm
Hotchkis & Wiley Small Cap Value

Mid-Sized Company Stock Funds
Artisan Mid Cap
Janus Mid Cap Value Investors

Large Company Stock Funds
American Funds Growth Fund A
Vanguard Equity-Income Adm
Vanguard Growth & Income Adm

Balanced Funds
Vanguard Balanced Index

Bond Funds
Vanguard Total Bond Market Index

Fixed Investment Options
DCRP Fixed Fund

Mutual fund administrative costs are not presented on the financial statements. Mutual fund earnings are generally declared net of expenses in accordance with the Securities Exchange Commission and other regulatory authorities. Current reporting standards for mutual companies do not require costs to be made available in the detailed cost reports.

The fixed investment option guarantees both principal (the deferred salary) and a quarterly rate of return. The fixed investment option requires the services of two external providers who were selected through the State's competitive bidding process. The external providers are: Aegon and Pacific Investment Management Company (PIMCO). Aegon provides a guarantee of principal for the fixed assets and sets a quarterly rate of return based upon the investment manager's portfolio yield and duration. PIMCO, the investment manager, directs the investment of fixed assets. Fixed assets are invested in the mutual market in accordance with established guidelines for credit quality, duration and issue concentration.

Fees on the fixed investments are charged by each of the providers. The fees are defined per each contract for specific services rendered. The record keeper, Great West, charges a fixed administrative fee for all plan participants plus a basis point (or percent) fee based on account balances. On a quarterly basis, the contracted record keeper withholds the fees from each plan participant's account. The basis point fees withheld are submitted to the PERB to pay administrative expenses. These amounts are recorded as *Miscellaneous Revenue* in the financial statements.

Administrative expenses and the revenues that fund them are accounted for within the plan. For the PERS-DCRP, the fixed investment is invested in a PIMCO mutual fund and all fees for investment expense are netted from the mutual fund earnings; therefore, the fees are not presented on our financial statements. The fees charged by Great West and Aegon are classified as *Miscellaneous Expense.*

A brief summary of eligibility and benefits follows:

PERS-DCRP Summary of Benefits

Eligibility for Benefit
Termination of service

Vesting
Immediate for member's contributions and attributable income;
5 years for a portion of employer's contributions and attributable income

Benefit
Dependent upon individual account balance;
IRS permitted rollovers are also possible

At June 30, 2006 PERS-DCRP had 229 reporting employers, one less than in FY2005. The participating employers consist of:

PERS-DCRP EMPLOYERS

Employers	June 30, 2006	June 30, 2005
State Agencies	29	27
Counties	43	46
Cities and Towns	41	40
Universities	5	5
School Districts	79	79
High Schools	2	0
Other Agencies	30	33
Total	229	230

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal year 2006 was 6.9% of PERS-covered payroll. Contributions are deducted from each member's salary and remitted by participating employers. The entire amount of the member's contribution is credited to the member's retirement account. An individual account is maintained by the third-party record keeper. Each state agency and university system employer contributed 6.9% of PERS-covered payroll during fiscal year 2006. Participating local governments and school district employers contribute 6.8% of PERS-covered payroll during fiscal year 2006. The State contributes the remaining 0.1% for local governments and school employers from the state general fund. The employer rate of 6.9% is allocated as follows: 4.19% allocated to the member's retirement account, 2.37% allocated to the defined benefit plan choice rate, 0.04% allocated to defined contribution education fund and 0.3% allocated to the long-term disability plan. (Reference Schedule of Contribution Rates on page 76).

Plan Membership Elections: Included in the financial statements are employer contribution transfers of $16,000 and member contribution transfers of $26,000. These transfers reflect the contribution transfers of DCRP participants that filed elections at or near the June 30 cutoff date but the contributions were moved in early fiscal year 2007.

PERS-DCRP Active Membership by Employer Type

Employer Type	June 30, 2006	June 30, 2005
State Agencies	579	467
Counties	265	230
Cities	183	156
Universities	57	44
High Schools	2	0
School Districts	172	158
Other Agencies	104	81
Total	1,362	1,136

DCRP Education Fund: Implemented July 1, 2002, the DCRP Education Fund (DCEd), as governed by section 19-3-112, MCA, provides education to the members that have joined the PERS-DCRP. The DCEd is funded by 0.04% of the employers' contributions.

DCRP Disability Fund: Implemented July 1, 2002, the DCRP Disability Fund (DC Disability), as governed by section 19-3-2117, MCA, will provide disability benefits to eligible members of the PERS-DCRP. The DC Disability is funded by 0.3% of the employers' contribution.

Deferred Compensation Plan (457)

Plan Description: The deferred compensation (457) plan is a voluntary supplemental retirement savings plan established in 1976. The deferred compensation plan is governed by Title 19, chapter 50, MCA, in accordance with Internal Revenue Service Code (IRC) §457. All employees of the State, the Montana University System and contracting political subdivisions, are eligible to participate.

Assets of the deferred compensation plan are required to be held in trusts, custodial accounts or insurance company contracts for the exclusive benefit of participants and their beneficiaries. Great West is the third-party record keeper for the deferred compensation plan. Participants elect to defer a portion of their salary, within Internal Revenue Code limits. The deferred salary is not available to employees until separation from service, retirement, death, or upon an unforeseeable emergency while still employed, provided IRS-specified criteria are met.

Plan participants direct their deferred salary into investment options offered within the plan. The investment options offered are selected by the PERB and pursuant to the plan's Investment Policy Statement, with the assistance of the statutorily-created Employee Investment Advisory Council and with the advice of a third-party investment analyst. Plan participants may invest in as many of the offered investment options as desired. The offered investment options fall into two primary types: (1) the fixed investment option and (2) the variable investment options. The variable investment options include mutual funds and profile funds. All options range from aggressive to conservative. The mutual funds cover all standard asset classes and categories. The profile funds are preset funds that invest in underlying mutual funds to achieve a set objective such as time horizon or investment style. The investment options as of June 30, 2006 are as follows:

Deferred Compensation (457) Plan
Investment Options

International Stock Funds

Artisan International
Mutual Discovery Z
Templeton Foreign A
American Funds New Perspective

Small Company Stock Funds

Neuberger Berman Genesis
RS Diversified Growth
Munder Small Cap Value

Mid-Sized Company Stock Funds

Artisan Mid Cap Investors
Hotchkis & Wiley Mid-cap Value

Large Company Stock Funds

Davis NY Venture A
Fidelity Contrafund

TCW Galileo Select Equities N
Vanguard 500 Index
Calvert Social Investors

Balanced Funds
Dodge & Cox Balanced

Bond Funds
Neuberger Berman High Income
PIMCO Total Return Admin

Fixed Investment Options
Montana Fixed Fund

Profile Funds
Aggressive
Moderately Aggressive
Moderate
Moderately Conservative
Conservative

Mutual fund administrative costs are not presented on the financial statements. Mutual fund earnings are generally declared net of expenses in accordance with the Securities Exchange Commission and other regulatory authorities. Current reporting standards for mutual companies do not require costs to be made available in the detailed cost reports.

The fixed investment option guarantees both principal (the deferred salary) and a quarterly rate of return. The fixed investment option requires the services of three external providers who were selected through the State's competitive bidding process. The external providers are: Aegon, Pacific Investment Management Company (PIMCO) and State Street Bank Kansas City (SSKC). Aegon provides a guarantee of principal and sets a quarterly rate of return based upon the investment manager's portfolio yield and duration. PIMCO, the investment manager, directs the investment of fixed assets. Fixed assets are invested in the bond market in accordance with established guidelines for credit quality, duration and issue concentration. SSKC is PIMCO's custodial bank and holder of the fixed assets. SSKC exchanges the assets as directed by PIMCO.

In addition to the above investment options, plan participants previously had the option to direct a portion of their deferrals to a term life insurance policy provided through Allianz Life Insurance. The ability to invest in life insurance is allowed under the IRC and was offered to plan participants prior to life insurance being offered as a standard component of health insurance benefit packages. This investment option has been discontinued; however, plan participants who had previously or originally elected this option may continue.

Fees on the fixed investments are charged by each of the three providers. The fees are defined per each contract for specific services rendered. The record keeper, Great West, charges a fixed administrative fee for all plan participants. The fixed record-keeping fee, by contract, is a flat dollar amount. On a quarterly basis, the contracted record keeper withholds the basis point fee from each plan participant's account. The basis point fees collected are reconciled to the contractual flat dollar amount and any fees withheld in excess of the contractual flat dollar fee are submitted to the PERB. Also submitted to the PERB are 12(b)(1) or re-allotment fees from certain mutual fund companies. These fees are normally charged by the mutual funds for the purpose of individual record keeping. Because the mutual fund companies involved in the deferred compensation plan do not need to keep records of participants' accounts, the fees are returned to the PERB. The PERB uses the excess and 12(b)(1) fees to pay administrative expenses associated with the deferred compensation plan. These amounts are recorded as *Miscellaneous Revenue.*

Administrative expenses and the revenues that fund them are accounted for within the plan. The fees charged by PIMCO and SSKC for the externally managed fixed investments are classified as *Investment Expense*. The fees charged by Great West and Aegon are classified as *Miscellaneous Expense*. A brief summary of eligibility and benefits follow:

Deferred Compensation Plan Summary

Contribution
Voluntary, tax-deferred

Eligibility of Benefit
Not available to participant until separation from service; retirement; death; or upon an unforeseeable emergency, while still employed, provided IRS-specified criteria are met.

Vesting
Participants are fully vest in their accounts at the time of deposit

Benefit
Lump sum or periodic benefit payment, at the option of the participant. Based on individual account balances and plan provisions. IRS permitted rollovers are also possible.

At June 30, 2006 the deferred compensation plan had 12 participating employers an increase, of two from FY 2005. The participating employers consist of:

DEFERRED COMPENSATION EMPLOYERS

Employers	June 30, 2006	June 30, 2005
State of Montana *	1	1
Counties	2	0
Colleges and Universities	6	6
School Districts	1	1
Other	2	2
Total	12	10

*The State of Montana includes 36 agencies; however, due to the nature of the reporting for the 457 plan we are unable to specifically determine which agencies participate.

Contributions: The deferred compensation plan is a voluntary, tax-deferred retirement plan designed to supplement retirement, Social Security and other retirement plans and savings. Participants designate the amount to contribute within IRC limitations. The deferred salary is withheld through payroll deduction prior to federal and state taxes. Social Security and Medicare taxes are withheld on the deferred salary. The contributions are either directed to the fixed investment or to any number of the available variable investments. The money designated as fixed is invested by PIMCO. The money designated as variable is remitted to the third-party record keeper who in turn invests the contributions in selected investments as directed by the participant.

FY 2006 Schedule of Contribution Rates

System	Member	Employer	State
PERS-DBRP	**6.9%** [19-3-315, MCA]	**6.9%** State & University **6.8%** Local Governments [19-3-316, MCA]	**0.1%** of local government payroll – paid from the General Fund [19-3-319, MCA]
PERS-DCRP	**6.9%** [19-3-315, MCA]	**6.9%** State & University **6.8%** Local Governments [19-3-316, MCA]	**0.1%** of local government payroll – paid from the General Fund [19-3-319, MCA]
JRS	**7.0%** [19-5-402, MCA]	**25.81%** [19-5-404, MCA]	
HPORS	**9.0%** - hired prior to 7-01-97 & not electing GABA **9.05%** - hired after 6-30-97 & members electing GABA [19-6-402, MCA]	**26.15%** [19-6-404(1), MCA] **10.18%** of salaries – paid from drivers' license fees [19-6-404(2), MCA]	
SRS	**9.245%** [19-7-403, MCA]	**9.535%** [19-7-404, MCA]	
GWPORS	**10.56%** [19-8-502, MCA]	**9.0%** [19-8-504, MCA]	
MPORS	**5.8%** - hired on or before 6-30-75 & not electing GABA [19-9-710(a), MCA] **7.0%** - hired after 6-30-75 & prior to 7-1-79 & not electing GABA [19-9-710(b), MCA] **8.5%** - hired after 6-30-79 and prior to 7-1-97 & not electing GABA [19-9-710(c), MCA] **9.0%** - hired after 6-30-97 & members electing GABA [19-9-710(d), MCA]	**14.41%** [19-9-703, MCA]	**29.37%** of salaries – paid from the General Fund [19-9-702, MCA]
FURS	**9.5%** - hired prior to 7-01-97 & not electing GABA [19-13-601(2)(a), MCA] **10.7%** - hired after 06-30-97 & members electing GABA [19-13-601(2)(b), MCA]	**14.36%** [19-13-605, MCA]	**32.61%** of salaries – paid from the General Fund [19-13-604, MCA]
VFCA			**5.0%** of fire insurance premiums, paid from the General Fund [19-17-301, MCA]

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Public Employees' Retirement Board

A Component Unit of the State of Montana

Required Supplementary Information

Schedule of Funding Progress

(in thousands)

System	Actuarial Valuation Date	Actuarial Value of Assets[1] (a)	Actuarial Accrued Liability (AAL) -Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
PERS-DBRP	06/30/02	$ 3,076,781	$ 3,077,764	$ 983	99.97%	$ 808,747	0.12%
	06/30/04	3,047,287	3,514,085	466,798	86.72	832,847	56.05
	06/30/05	3,179,010	3,719,998	540,988	85.46	847,431	63.84
	06/30/06	**3,459,084**	**3,919,313**	**460,229**	**88.26**	**880,708**	**52.26**
JRS	06/30/02	44,963	30,882	(14,081)	145.60	4,000	-352.03
	06/30/04	45,134	34,724	(10,410)	129.98	4,403	-236.43
	06/30/05	47,552	34,525	(13,027)	137.73	4,462	-291.95
	06/30/06	**51,808**	**37,159**	**(14,649)**	**139.42**	**4,762**	**-307.62**
HPORS	06/30/02	81,734	94,850	13,116	86.17	7,536	174.04
	06/30/04	79,104	104,069	24,965	76.01	7,844	318.27
	06/30/05	82,050	112,938	30,888	72.65	9,104	339.28
	06/30/06	**87,189**	**112,002**	**24,813**	**77.85**	**7,878**	**314.97**
SRS	06/30/02	138,590	121,625	(16,965)	113.95	24,521	-69.19
	06/30/04	141,022	148,608	7,586	94.90	27,373	27.71
	06/30/05	148,458	159,347	10,889	93.17	28,423	38.31
	06/30/06	**163,003**	**171,841**	**8,838**	**94.86**	**34,242**	**25.81**

Analysis of the dollar amounts of plan net assets, actuarial accrued liability, and unfunded actuarial accrued provides one indication of the plan's funding status on a going-concern basis. Analysis of this percentage percentage, the stronger the plan. Trends in the unfunded actuarial accrued liability and annual covered covered payroll approximately adjusts for the effects of inflation and aids analysis of the plan's progress stronger the plan.

[1]Refer to the "Notes to the Required Supplementary Information" for the Actuarial Asset Valuation Method (Page A-72).

[2]This schedule reflects a subsequent letter from Milliman, MPERA's actuary, dated January 20, 2003. If the actual rates of termination were used for the corrections officers that transferred into the GWPORS the Funded Status of the system would have been a slight Actuarial Surplus rather than a slight Unfunded Actuarial Liability.

System	Actuarial Valuation Date	Actuarial Value of Assets [1] (a)	Actuarial Accrued Liability (AAL) -Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
GWPORS	06/30/02[2]	38,730	38,340	(390)	101.02%	17,151	-2.27%
	06/30/04	45,210	50,310	5,100	89.86	21,442	23.79
	06/30/05	50,961	56,414	5,453	90.33	22,496	24.24
	06/30/06	**58,813**	**64,183**	**5,370**	**91.63**	**25,846**	**20.78**
MPORS	06/30/02	143,516	226,827	83,311	63.27	22,229	374.79
	06/30/04	149,510	260,094	110,584	57.48	24,531	450.79
	06/30/05	159,417	276,379	116,962	57.68	26,198	446.45
	06/30/06	**175,919**	**291,099**	**115,180**	**60.43**	**27,644**	**416.65**
FURS	06/30/02	136,392	197,946	61,554	68.90	17,953	342.86
	06/30/04	142,109	227,599	85,490	62.44	20,248	422.21
	06/30/05	151,393	238,157	86,764	63.57	20,474	423.78
	06/30/06	**167,343**	**255,513**	**88,170**	**65.49**	**22,917**	**384.74**
VFCA	06/30/02	19,254	26,808	7,554	71.82	N/A	N/A
	06/30/04	20,058	28,680	8,622	69.94	N/A	N/A
	06/30/05	21,311	30,773	9,462	69.25	N/A	N/A
	06/30/06	**23,238**	**31,883**	**8,645**	**72.89**	**N/A**	**N/A**

Covered payroll is not applicable to VFCA because members are unpaid volunteers.

liability in isolation can be misleading. Expressing plan net assets as a percentage of the actuarial accrued liability over time indicates whether the plan is becoming financially stronger or weaker. Generally, the greater this payroll are both affected by inflation. Expressing the unfunded actuarial accrued liability as a percentage of annual made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the

Public Employees' Retirement Board

A Component Unit of the State of Montana

Required Supplementary Information

Schedule of Employer Contributions & Other Contributing Entities

System	Year Ended June 30	Annual Required Contributions	Actuarial Required Contribution Rate[1]	Percentage Contributed	Annual Required State Contribution[2]	Percentage Contributed
PERS-DBRP	2001	$ 29,238,994	3.79%	181.98%	$ 382,481	100.00%
	2002	55,803,545	6.90	99.54	373,721	100.00
	2003	58,573,696	6.90	98.16	388,954	100.00
	2004	67,044,215	8.05	86.20	402,566	100.00
	2005	71,523,156	8.44	82.06	420,658	100.00
	2006	**69,311,689**	**7.87**	**91.54**	**442,994**	**100.00**
JRS	2001	638,282	17.46	147.82		
	2002	801,137	20.03	128.86		
	2003	816,691	20.03	128.86		
	2004	304,277	6.91	373.52		
	2005	143,222	3.21	811.43		
	2006	**112,854**	**2.37**	**1,089.03**		
HPORS	2001	637,399	8.67	414.48	335,107	100.00
	2002	2,737,999	36.33	101.16	308,973	100.00
	2003	2,836,992	36.33	101.02	353,589	100.00
	2004	2,849,545	36.33	100.32	348,137	100.00
	2005	3,307,439	36.33	100.50	668,748	100.00
	2006	**2,862,188**	**36.33**	**101.50**	**277,178**	**100.00**
SRS	2001	1,672,537	7.39	133.17		
	2002	2,338,104	9.54	102.10		
	2003	2,435,269	9.54	102.70		
	2004	3,198,485	11.69	84.57		
	2005	3,474,750	12.23	80.95		
	2006	**3,896,731**	**11.38**	**90.42**		

Refer to the "Notes to the Required Supplementary Information" (Page A-72).

This schedule was revised in FY2005 to reflect the actuarially calculated ARC rather than the statutory rate that was previously used.

[1] The Annual Required Contribution for FY01 and FY03 is based on prior year-end actuarial study.

[2] The Annual Required Contribution for HPORS includes the required registration fees and for MPORS and FURS is based on covered payroll, which includes payroll adjustments.

System	Year Ended June 30	Annual Required Contributions	Actuarial Required Contribution Rate[1]	Percentage Contributed	Annual Required State Contribution[2]	Percentage Contributed
GWPORS	2001	$ 805,073	5.41%	169.66%		
	2002	1,759,644	10.26	90.64		
	2003	2,055,590	10.26	89.28		
	2004	1,979,117	9.23	102.12		
	2005	2,083,154	9.26	98.58		
	2006	**2,336,515**	**9.04**	**102.34**		
MPORS	2001	3,011,475	14.41	100.12	$ 6,137,893	100.16%
	2002	3,203,173	14.41	102.15	6,528,604	100.02
	2003	3,355,991	14.41	104.89	6,840,073	99.39
	2004	3,534,920	14.41	102.68	7,204,760	100.05
	2005	3,775,191	14.41	100.41	7,694,474	100.14
	2006	**3,983,471**	**14.41**	**101.30**	**8,118,982**	**100.77**
FURS	2001	2,401,328	14.36	98.81	5,453,155	98.45
	2002	2,578,021	14.36	97.80	5,854,406	98.46
	2003	2,672,133	14.36	106.04	6,068,123	98.98
	2004	2,876,584	14.36	100.09	6,532,410	100.00
	2005	2,940,092	14.36	100.65	6,676,629	100.63
	2006	**3,290,840**	**14.36**	**101.14**	**7,473,141**	**100.80**
VFCA	2001				1,002,992	100.00
	2002				1,133,741	100.00
	2003				1,310,088	100.00
	2004				1,434,068	100.00
	2005				1,527,264	100.00
	2006				**1,610,462**	**100.00**

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of latest actuarial valuation follows:

	PERS-DBRP	JRS	HPORS
Valuation date	June 30, 2006	June 30, 2006	June 30, 2006
Actuarial cost method	Entry Age	Entry Age	Entry Age
Amortization method	Level percentage of payroll, open	Level percentage of payroll, open	Level percentage of payroll, open
Remaining amortization period in years:			
Unfunded Liability	does not amortize[1]		18
Unfunded Credit [2]		30	
Asset valuation method	4-Year smoothed market	4-Year smoothed market	4-Year smoothed market
Actuarial assumptions:			
Investment rate of return compounded annually	8%	8%	8%
Projected salary increases			
General Wage Growth*	4.25%	4.25%	4.25%
Merit	0% - 6%	None	0% - 7.3%
* includes inflation rate at	3.25%	3.25%	3.25%
Benefit Adjustments			
GABA	3% after 1 yr	3% after 1 yr	3% after 1 yr
Non-GABA	N/A	Annual increase to salary of active member in like position	2% per yr service for newly confirmed officer

[1] The amortization period for the unfunded actuarial liability in the PERS and SRS exceeds 40 years. The amortization period for the unfunded actuarial liability for GWPORS is 32.4 years. Based on actuarial assumptions as of June 30, 2006, additional funding is required at a rate of 1.01% for PERS, 1.84% for SRS and .04% for GWPORS. The PERB anticipates legislation to be enacted within fiscal year 2007 to actuarially fund the systems.

[2] Assets are larger than the past service liability – creating an unfunded credit; the credit is amortized over future costs.

SRS	GWPORS	MPORS	FURS	VFCA
June 30, 2006	June 30, 2006	June 30, 2006	June 30, 2006	June 30, 2006
Entry Age	Entry Age	Entry Age	Entry Age	Entry Age
Level percentage of payroll, open	Level percentage of payroll, open	Level percentage of payroll, open	Level percentage of payroll, open	Level percentage of revenue, open
does not amortize[1]	32.4 [1]	21.4	15.5	20
4-Year smoothed market	4-Year smoothed market	4-Year smoothed market	4-Year smoothed market	4-Year smoothed market
8%	8%	8%	8%	8%
4.25%	4.25%	4.25%	4.25%	N/A
0% - 7.3%	0% - 7.3%	0% - 7.3%	0% - 7.3%	N/A
3.25%	3.25%	3.25%	3.25%	N/A
3% after 1 yr	3% after 1 yr	3% after 1 yr	3% after 1 yr	N/A
N/A	N/A	50% newly confirmed officer	50% newly confirmed officer	N/A

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Public Employees' Retirement Board

A Component Unit of the State of Montana

Schedule of Administrative Expenses

Year Ended June 30, 2006

	Defined Benefit Plans	PERS-DBRP Education Fund	Defined Contribution PERS-DCRP	Deferred Compensation 457 Plan
Personal Services				
Salaries	$ 1,110,828	$ 105,216	$ 66,206	$ 66,481
Board Members' Per Diem	8,187		432	432
Employee Benefits	319,145	31,335	19,872	19,234
Total Personal Services	1,438,160	136,551	86,510	86,147
Other Services				
Consulting Services	417,570	191	27,184	29,741
Legal Fees and Court Costs	24,547		178	178
Payroll Fees	973	82	75	65
Audit Fees	32,047		1,023	1,023
Medical Services	13,199			
Records Storage	9,134	21		
Pre-Retirement Seminars		3,000		
Computer Processing	296,193	2,748	10,811	6,752
Printing and Photocopy Charges	21,077	30,768	965	1,245
Warrant Writing Services	35,004		1,117	1,117
Other	8,283	698	639	552
Total Other Services	858,027	37,508	41,992	40,673
Communications				
Recruitment Costs	8,069	201	781	704
Postage and Mailing	82,837	14,768	1,138	5,761
Telephone	24,357	2,644	1,771	1,540
Total Communications	115,263	17,613	3,690	8,005
Other Expenses				
Supplies and Materials	49,206	7,061	3,090	2,128
Travel	38,648	8,462	3,677	3,649
Rent	185,863	17,668	14,347	12,391
Repairs and Maintenance	432	36	33	29
Depreciation/Amortization	294,099	114	3,305	47,563
Compensated Absences	(20,434)	4,601	1,543	(413)
Interest Payments			57,441	
Miscellaneous	44,036	(4,401)	11,542	3,555
Total Other Expenses	591,850	33,541	94,978	68,902
Total Administrative Expenses	**$ 3,003,300**	**$ 225,213**	**$ 227,170**	**$ 203,727**

Schedule of Investment Expenses

Year Ended June 30, 2006

Plan	Investment Manager	Fees
PERS-DBRP	Board of Investments	$ 5,008,119
JRS	Board of Investments	72,823
HPORS	Board of Investments	125,327
SRS	Board of Investments	227,403
GWPORS	Board of Investments	76,494
MPORS	Board of Investments	237,074
FURS	Board of Investments	225,582
VFCA	Board of Investments	31,538
457	PIMCO	418,871
	State Street Bank	54,551
Total Investment Expense		**$ 6,477,782**

Public Employees' Retirement Board

A Component Unit of the State of Montana

Schedule of Consultants

Year Ended June 30, 2006

Individual or Firm	Nature of Service	Amount Paid
Wisetek Provider Inc	Web Reporting Systems Development	$ 213,745
Amdec Software	Computer Programming Services	165,060
Milliman	Actuarial Consultant	77,691
Americh Massena & Associates, Inc.	Mutual Funds Performance Review	37,900
Legislative Audit Division, Legislative Branch	Independent Auditors	34,093
Ice Miller	Tax Consultant	26,433
Communications & Management Service	Human Resources Consulting	11,325
Lawrence R. McEvoy, MD	Medical Consultant	7,418
Legal Services Division, Department of Justice	Legal Services	6,512
Goetz, Gallik, Baldwin & Dolan	Legal Services	4,217
Professional Development Center, Department of Administration	Retirement Planning Seminars	3,000

Public Employees' Retirement Board

A Component Unit of the State of Montana

Detail of Fiduciary Net Assets (PERS-DBRP and PERS-DBEd)

as of June 30, 2006

	PERS-DBRP	PERS-DBEd	TOTAL
Assets			
Cash and Short-term Investments	$ 92,501,686	$ 1,187,246	$ 93,688,932
Securities Lending Collateral	67,406,590	19,345	67,425,935
Receivables			
Interest	7,173,427		7,173,427
Accounts Receivable	1,223,670	8	1,223,678
Due from Other Funds	316,196	7,642	323,838
Due from Primary Government	28,811		28,811
Due from Component Unit	1,995		1,995
Notes Receivable	135,357		135,357
Total Receivables	8,879,456	7,650	8,887,106
Investments, at fair value			
Montana Domestic Equity Pool (MDEP)	1,586,747,062		1,586,747,062
Retirement Fund Bond Pool (RFBP)	932,047,876		932,047,876
Montana International Pool (MTIP)	630,135,329		630,135,329
Montana Private Equity Pool (MPEP)	203,406,134		203,406,134
Montana Real Estate Pool (MTRP)	15,200,000		15,200,000
Real Estate Investments	8,636,356		8,636,356
Mortgages & Commercial Loans net of Accumulated Mortgage Discount	43,096,807		43,096,807
Total Investments	3,419,269,564		3,419,269,564
Capital Assets			
Property and Equipment, at cost, net of Accumulated Depreciation	513		513
Intangible Assets, at cost, net of Amortization Expense	102,626	432	103,058
Total Capital Assets	103,139	432	103,571
Total Assets	3,588,160,435	1,214,673	3,589,375,108
Liabilities			
Securities Lending Collateral Liability	67,406,590	19,345	67,425,935
Accounts Payable	495,023	7,570	502,593
Due to Other Funds	93,863	364	94,227
Due to Primary Government	45,866	4,269	50,135
Deferred Revenue	70,942		70,942
Compensated Absences	233,019	15,581	248,600
Total Liabilities	68,345,303	47,129	68,392,432
Net Assets Held in Trust for Pension Benefits	**$ 3,519,815,132**	**$ 1,167,544**	**$ 3,520,982,676**

Public Employees' Retirement Board

A Component Unit of the State of Montana

Detail of Changes in Fiduciary Net Assets (PERS-DBRP and PERS-DBEd)

for the Fiscal Year Ended June 30, 2006

	PERS-DBRP	PERS-DBEd	TOTAL
Additions			
Contributions			
Employer	$ 63,089,060	$ 356,354	$ 63,445,414
Plan Member	66,002,308		66,002,308
Membership Fees	83		83
Interest Reserve Buyback	143,047		143,047
Retirement Incentive Program	123,784		123,784
Miscellaneous Revenue	25,003,468	137	25,003,605
State Contributions	442,994		442,994
Total Contributions	154,804,744	356,491	155,161,235
Investment Income			
Net Appreciation (Depreciation) in Fair Value of Investments	185,484,598		185,484,598
Interest	98,875,075	46,199	98,921,274
Dividends	14,161,359		14,161,359
Investment Expense	(5,008,119)		(5,008,119)
Net Investment Income	293,512,913	46,199	293,559,112
Securities Lending Income			
Securities Lending Income	5,129,851	805	5,130,656
Securities Lending Rebate and Fees	(5,010,361)	(802)	(5,011,163)
Net Securities Lending Income	119,490	3	119,493
Total Net Investment Income	293,632,403	46,202	293,678,605
Total Additions	448,437,147	402,693	448,839,840
Deductions			
Benefits	153,885,649		153,885,649
Refunds/Distributions	12,753,802		12,753,802
Refunds to Other Plans	568,003		568,003
Transfers to DCRP	1,064,447		1,064,447
Transfers to ORP	183,135		183,135
Administrative Expenses	2,661,191	225,213	2,886,404
Total Deductions	171,116,227	225,213	171,341,440
Net Increase (Decrease)	277,320,920	177,480	277,498,400
Net Assets Held in Trust for Pension Benefits			
Beginning of Year	**3,242,428,809**	**990,064**	**3,243,418,873**
Prior Period Adjusment	**65,403**		**65,403**
End of Year	**$ 3,519,815,132**	**$ 1,167,544**	**$ 3,520,982,676**

Public Employees' Retirement Board

A Component Unit of the State of Montana

Detail of Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and PERS-DC Disability)

as of June 30, 2006

	PERS-DCRP	PERS-DCEd	PERS-DC DISABILITY	TOTAL
Assets				
Cash and Short-term Investments	$ 507,485	$ 65,227	$ 451,619	$ 1,024,331
Securities Lending Collateral	5,876	1,064	7,389	14,329
Receivables				
Due from Other Funds	91,431	364	2,440	94,235
Total Receivables	91,431	364	2,440	94,235
Investments, at fair value				
Defined Contributions Fixed Investments	1,832,487			1,832,48[illegible]
Defined Contributions Variable Investments	29,101,644			29,101,644
Total Investments	30,934,131			30,934,131
Intangible Assets, at cost, net of Amortization Expense	2,215			2,215
Total Assets	31,541,138	66,655	461,448	32,069,241
Liabilities				
Securities Lending Collateral Liability	5,876	1,064	7,389	14,329
Accounts Payable	7,435	362		7,797
Due to Other Funds	2,364	8,388		10,752
Due to Primary Government	21,308			21,308
Due to Component Unit	24,248			24,248
Advances from Primary Government	1,360,195			1,360,195
Compensated Absences	9,311	1,033		10,344
Total Liabilities	1,430,737	10,847	7,389	1,448,973
Net Assets Held in Trust for Pension Benefits	**$ 30,110,401**	**$ 55,808**	**$ 454,059**	**$ 30,620,268**

Public Employees' Retirement Board

A Component Unit of the State of Montana

Detail of Changes in Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and PERS-DC Disability)

for the Fiscal Year Ended June 30, 2006

	PERS-DCRP	PERS-DCEd	PERS-DC DISABILITY	TOTAL
Additions				
Contributions				
Employer	$ 2,143,543	$ 25,930	$ 149,694	$ 2,319,167
Plan Member	3,699,360			3,699,360
Miscellaneous Revenue	223,324			223,324
Forfeiture of Nonvested Member	263,685			263,685
Total Contributions	6,329,912	25,930	149,694	6,505,536
Investment Income				
Net Appreciation (Depreciation) in Fair Value of Investments	991,131			991,131
Interest	1,088,646	2,341	15,607	1,106,594
Net Investment Income	2,079,777	2,341	15,607	2,097,725
Securities Lending Income				
Securities Lending Income	190	41	272	503
Securities Lending Rebate and Fees	(189)	(41)	(271)	(501)
Net Securities Lending Income	1	0	1	2
Total Net Investment Income	2,079,778	2,341	15,608	2,097,727
Total Additions	8,409,690	28,271	165,302	8,603,263
Deductions				
Refunds/Distributions	1,570,066			1,570,066
Administrative Expenses	213,706	13,464		227,170
Miscellaneous Expenses	295,105			295,105
Total Deductions	2,078,877	13,464	-	2,092,341
Net Increase (Decrease)	6,330,813	14,807	165,302	6,510,922
Net Assets Held in Trust for Pension Benefits				
Beginning of Year	23,779,588	41,001	288,757	24,109,346
Prior Period Adjustment				-
End of Year	**$ 30,110,401**	**$ 55,808**	**$ 454,059**	**$ 30,620,268**

Board Response

PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION

BRIAN SCHWEITZER
GOVERNOR

STATE OF MONTANA

mpera.mt.gov

HELENA (406) 444-3154
TOLL FREE (877) 275-7372
FAX (406) 444-5428

100 N. PARK, SUITE 200
PO BOX 200131
HELENA, MT 59620-0131

November 30, 2006

RECEIVED
DEC 0 4 2006
LEGISLATIVE AUDIT DIV.

Scott A. Seacat, Legislative Auditor
Legislative Audit Division
Room 160, State Capitol
PO Box 201705
Helena MT 59620-1705

Dear Mr. Seacat,

We appreciate the opportunity to respond to the recommendations in the Financial-Compliance Audit of the Public Employees' Retirement Board (PERB) for two fiscal years ended June 30, 2006.

Recommendation #1
We recommend legislation be enacted for funding changes to ensure the PERS-DBRP, SRS, and the GWPORS are funded on an actuarially sound basis, as required by the Montana Constitution and state law.

Response
We concur. Public retirement systems are required by the Montana Constitution, State statute and the PERB's Benefit and Funding Policy to be actuarially sound. If retirement systems are determined not to be actuarially sound, action is required by the legislature to attain the actuarial soundness of all public retirement systems. Other impacts of the systems not being actuarially sound include: non-compliance with the Governmental Accounting Standards Board and possible adverse effects on the State of Montana's bond rating.

According to the PERB's Actuarial Valuations as of June 30, 2004, June 30, 2005 and June 30, 2006 the PERS-DBRP, SRS and GWPORS are actuarially unsound. In response to the June 30, 2004 Valuations, the PERB submitted House Bill 148 to the 2005 legislative session and tried to submit a bill to the 2005 special session based on data from the June 30, 2005 Valuations. Both attempts were unsuccessful. Based on the June 30, 2006 Actuarial Valuations, the PERB has once again submitted legislation that addresses this recommendation for the 2007 legislative session.

The PERB's proposed legislation, LC285, received approval from the State Administration and Veterans' Affairs Interim Committee (SAVA). SAVA is an interim committee that on April 27, 2005, was assigned to perform a legislative study on how public employee retirement funds are invested and how investment performance, retirement plan benefits, and legislative policy decisions interact to affect the actuarial soundness of the public employee retirement plans and employer's funding obligations. We believe the legislature is becoming more aware of the critical need to ensure that the systems are actuarially funded and are confident they will respond accordingly.

Recommendation #2

PERB has unreconciled balances identified between the external investment reports and balances recorded on SABHRS for the defined contribution plans it administers.

Response

We concur. MPERA has plans in place to balance to the vendors and has made great strides in our reconciliation process since the 2004 audit recommendation. The plan is being worked one step at a time. The reconciliations to the variable funds are complete.

Remaining in our work plan is balancing the fixed funds to the vendors. Turnover in personnel for the DC accountant position has resulted in slower progress than anticipated. The vendors each provide unique services and their relations to MPERA and each other are complicated. It takes time to learn and comprehend the relationships, the vendors' different reporting systems (all industry-accepted) and the respective information provided. The State's liability to plan members participating in the fixed funds is guaranteed - there is no risk to participants concerning the security of their fixed account balances. Currently, MPERA staff is working to balance to the remaining vendors and we anticipate a timely resolution to this issue.

We appreciate the professionalism demonstrated by the audit staff. Thank you for your assistance.

Sincerely,

Roxanne M. Minnehan

Roxanne M. Minnehan
Executive Director